

Exhibit A

Part 1 of 3



FORM 424B4

BigBand Networks, Inc. - BBND

Filed: March 15, 2007 (period:)

Form of prospectus disclosing information facts events covered in both forms 424B1 424B3

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Filed Pursuant to Rule 424(B)(4)
Registration No. 333-139652

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PROSPECTUS

10,700,000 Shares



COMMON STOCK

BigBand Networks, Inc. is offering 7,500,000 shares of its common stock and the selling stockholders are offering 3,200,000 shares of common stock. This is our initial public offering and no public market currently exists for our shares.

Our common stock has been approved for listing on the NASDAQ Global Market under the symbol "BBND."

Investing in our common stock involves risks. See "Risk Factors" beginning on page 7.

PRICE \$13 A SHARE

	<i>Price to Public</i>	<i>Underwriting Discounts and Commissions</i>	<i>Proceeds to BigBand</i>	<i>Proceeds to Selling Stockholders</i>
<i>Per Share</i>	<i>\$13.00</i>	<i>\$0.91</i>	<i>\$12.09</i>	<i>\$12.09</i>
<i>Total</i>	<i>\$139,100,000</i>	<i>\$9,737,000</i>	<i>\$90,675,000</i>	<i>\$38,688,000</i>

The selling stockholders have granted the underwriters the right to purchase up to an additional 1,605,000 shares of common stock to cover over-allotments. We will not receive any proceeds from the sale of shares by the selling stockholders.

The Securities and Exchange Commission and state securities regulators have not approved or disapproved these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The underwriters expect to deliver the shares to purchasers on March 20, 2007.

*MORGAN STANLEY
JEFFERIES & COMPANY*

MERRILL LYNCH & CO.

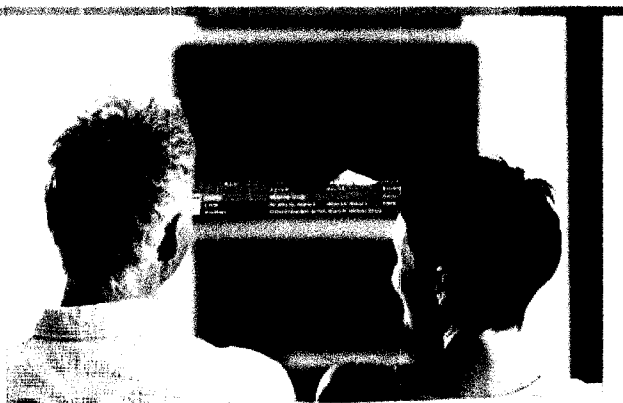
COWEN AND COMPANY

THINKEQUITY PARTNERS LLC

March 14, 2007

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BigBand Networks Enhances the Service Provider Triple Play



Video

Today's consumers are demanding increasingly rich, interactive and personalized video content. Video provides the most engaging user experience and generates the most revenue of any service in the triple play bundle, yet is the most challenging to deliver. BigBand Networks' video innovation makes new video services possible, including expanded broadcast, on-demand and high definition programming choices and advertising addressed to specific, relevant audiences.



Voice

BigBand Networks supports stringent telephony standards for reliability and quality.

Data

BigBand Networks accelerates broadband access speeds to enhance interactive experiences, such as online video.

Endband Networks enables service providers to offer Triple Play (video, voice and data) services to tens of millions of subscribers. Our key product applications include:

Efficient Video Delivery

Enables service providers to transmit video programming only when subscribers in a neighborhood are actually watching channels. By more efficiently delivering video content, operators can use reclaimed bandwidth to deliver an expanded number of channels, new services and personalized advertising.

Efficient Voice

Allows telephone companies to leverage existing infrastructure to add video programming. Service providers can provide a very high quality calling experience while benefiting from the use of digital transport throughout a network.

Efficient Video Migration

Enables service providers to cost-effectively migrate from and to digital video and overcome video quality limitations inherent in transporting analog over long distances.

Efficient Service

Allows service providers to deliver triple services that meet demanding quality and reliability standards.

Efficient Service Delivery

Service providers can offer real-time services, such as voice over IP, high speed data and streaming video content over the internet.



BIGBAND
networks

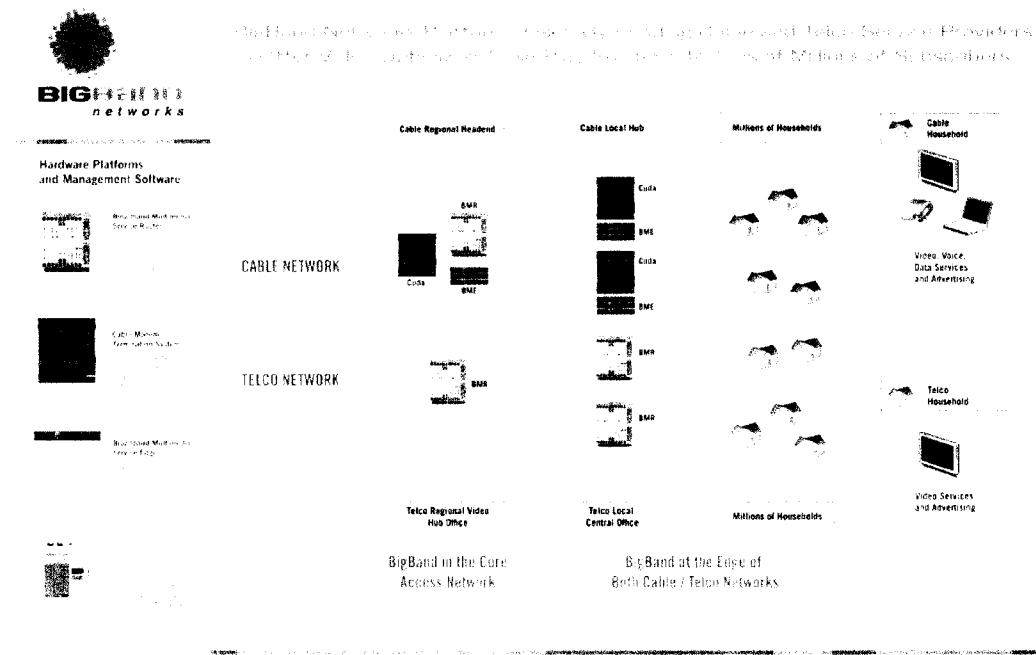
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You should rely only on the information contained in this prospectus or in any free writing prospectus we may authorize to be delivered or made available to you. Neither we nor the selling stockholders have authorized anyone to provide you with information different from that contained in this prospectus. We and the selling stockholders are offering to sell, and seeking offers to buy, shares of our common stock only in jurisdictions where offers and sales are permitted. The information in this prospectus is accurate only as of the date of this prospectus, regardless of the time of delivery of this prospectus or any sale of shares of our common stock.

Until April 8, 2007 (25 days after the commencement of this offering), all dealers that buy, sell or trade shares of our common stock, whether or not participating in this offering, may be required to deliver a prospectus. This delivery requirement is in addition to the obligation of dealers to deliver a prospectus when acting as underwriters and with respect to their unsold allotments or subscriptions.

For investors outside the United States: Neither we nor any of the selling stockholders nor any of the underwriters have done anything that would permit this offering or possession or distribution of this prospectus in any jurisdiction where action for that purpose is required, other than in the United States. Persons outside the United States who come into possession of this prospectus must inform themselves about, and observe any restrictions relating to, the offering of the shares of common stock and the distribution of this prospectus outside of the United States.

BigBand Networks, BME, BMR, Cuda, FastFlow and RateShaping are trademarks of BigBand Networks in the United States and other countries. This prospectus also includes other trademarks of BigBand and trademarks of other persons.

Table of Contents**PROSPECTUS SUMMARY**

This summary highlights information contained elsewhere in this prospectus and does not contain all of the information you should consider in making your investment decision. Before deciding to invest in shares of our common stock, you should read this summary together with the more detailed information, including our consolidated financial statements and the related notes, elsewhere in this prospectus. You should carefully consider, among other things, the matters discussed in "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations," in each case included elsewhere in this prospectus.

BIGBAND NETWORKS, INC.

We develop, market and sell network-based platforms that enable cable operators and telephone companies, collectively called service providers, to offer video, voice and data services across coaxial, fiber and copper networks. We have significant expertise in rich media processing, communications networking and bandwidth management. We have delivered what we believe to be the only successful commercial deployments of switched broadcast, an application that substantially increases the volume of content that a service provider can offer. In addition, we were the first to implement what we believe has become the industry's de facto network architecture for digital simulcast, an application that facilitates the insertion of advertising and the transmission of video in a digital format across a network while still providing service to analog subscribers. Our product applications of Digital Simulcast, TelcoTV, Switched Broadcast, and High-Speed Data and Voice-over-IP are a combination of our modular software and programmable video and data hardware platforms.

Our software and hardware product applications are used by leading service providers worldwide to offer video, voice and data services to tens of millions of subscribers, 24 hours a day, seven days a week. We have sold our product applications to more than 100 customers globally, including Cablevision, Charter, Comcast, Cox, Time Warner Cable and Verizon, which are six of the ten largest service providers in the United States. Our net revenues increased 80.3% to \$176.6 million for the year ended December 31, 2006 from \$98.0 million in 2005. We have been profitable on a quarterly basis since the three months ended September 30, 2006, and we first achieved profitability on an annual basis in 2006.

Intelligent, High-Bandwidth Video Networks Are Needed

Service providers derive most of their revenue from consumer subscriptions and advertising. Service providers are increasingly bundling disparate video, voice and data services into integrated offerings, also known as "triple-play" services. Video is the most technically demanding, provides the richest user experience and currently offers the greatest revenue per subscriber of the triple-play services. As of December 2006, Yankee Group Research estimates that, on average, consumers spend \$68 per month for digital video services compared to \$47 for voice and \$33 for data services.

Competition to deliver video, voice and data services has fueled recurring cycles of network investment as service providers seek to capture increasing revenues by offering additional services. Regulatory, technological and competitive factors are leading service providers to increasingly compete against one another for consumer subscription and advertising revenues. For example, cable operators have added approximately eight million voice-over-IP subscribers, while telephone companies are investing in video, such as Verizon's announced plan to upgrade its fiber-optic network for video and data services at a cost of \$18 billion. In addition to competing among themselves, service providers are facing competition from Internet and media companies, such as ABC.com, Apple Computer, Google and Yahoo, which use the Internet to deliver video content and advertising directly to consumers.

To differentiate their video, voice and data services from the competition, service providers are beginning to develop differentiated video offerings that more directly respond to consumer demand for more personalized and

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richer content, a higher quality experience and greater ease of access to this content. For example, subscribers are demanding more high definition television, or HDTV, and gaining more control over their consumption of video content through video-on-demand, or VOD, technologies. At the same time, advertisers are increasingly demanding that video-based advertising deliver more relevant ads with the interactivity to measure return on ad spending comparable to ads placed on the Internet. The need to respond to consumer demands for richer, more accessible and more relevant content, and advertisers' demands for increased interactivity, is forcing service providers to improve their networks.

Current service provider networks are not well suited to deliver the entire triple-play bundle of services and relevant advertising. In particular, these networks lack sufficient bandwidth necessary to deliver rich video services such as HD programming and lack the interactivity and ability to tailor programming and advertising to subscribers. As a result, a simple expansion of network capacity is not likely to meet these challenges, and there is a need for platforms designed primarily for reliable and cost-effective video delivery, which in turn will enable the entire triple-play offering. The rapidly changing trends in consumer demands and advertiser requirements, coupled with the competitive environment, are forcing service providers to develop more intelligent, extensible networks to provide these advanced services, enable increasingly relevant advertising and make more efficient use of available network capacity.

The BigBand Solution

The limitations of existing networks pose significant challenges to service providers. The BigBand solution addresses these challenges by enabling service providers to deliver high-quality video, voice and data services and more effective video advertising.

- *Intelligent Bandwidth Management.* The growing volume and richness of video content being demanded by subscribers, such as HDTV, is straining the capacity of existing fixed-bandwidth networks. Our media processing capabilities significantly increase the capacity of these networks without a costly capital expansion.
- *High-Quality Video Experience.* Video is less tolerant of the delays and errors that degrade the quality of the viewing experience. Our product applications enhance video quality in the network by correcting errors before subscribers are impacted.
- *Enhanced Video Personalization.* Networks lack the intelligence to understand and react to subscriber television viewing behavior. Using our product applications, service providers interact with their subscribers down to the individual channel change and, as a result, can more accurately tailor programming packages to the interests of their subscribers.
- *Ability to Deliver Relevant Video Advertising.* Existing networks provide only limited ability to deliver more relevant ads to audiences. Our products allow service providers to insert advertising tailored to specific geographic zones.
- *Optimize Return on Existing Infrastructure Investment.* Service providers have spent billions to build and maintain their networks and want to extend the useful life of their infrastructure investments. Our network-based products allow service providers to manage service quality and upgrade their voice, video and data offerings from the network, avoiding costly upgrades and installations of customer premise equipment, or CPE.
- *Platform Flexibility.* Networks must have the flexibility to rapidly deploy new services, such as HDTV, VOD and voice-over-IP, or VoIP. Our fully programmable hardware and modular software architecture is field-upgradable and designed to meet service provider requirements for network flexibility.

Table of Contents**Competitive Strengths of BigBand**

We have core expertise in media processing, communications networking and bandwidth management. We hold 26 U.S. patents, 16 of which relate to our video products and ten of which relate to our data products. Our expertise in emerging technologies, such as switched broadcast, and our customer relationships with large service providers are key strengths that enable us to gain greater insight into the network requirements of our customers. Leveraging this expertise, we combine our fully programmable hardware and modular software architecture to deliver product applications designed to meet service provider needs for intelligent, high-bandwidth networks. Our products are interoperable with a broad range of content and services in various parts of a service provider's network. Further, we believe our product applications decrease our customers' total cost of ownership, reduce their time-to-market with new services and improve their ability to achieve more efficient bandwidth utilization.

Risk Factors

Our business is subject to numerous risks, which are highlighted in the section entitled "Risk Factors" immediately following this prospectus summary. Some of these risks are:

- we depend on the adoption of advanced technologies by service providers for substantially all of our net revenues;
- our customer base is highly concentrated, and there are a limited number of potential customers for our products;
- the timing of a significant portion of our revenue is dependent on complex systems integration;
- our operating results are likely to fluctuate significantly for a variety of reasons; and
- our operating results in a particular period can be impacted by our lengthy sales cycle.

For further discussion of these and other risks you should consider before making an investment in our common stock, see the section entitled "Risk Factors" immediately following this prospectus summary.

Corporate Information

Our company was founded in December 1998, and through 2001 we were engaged principally in research and development on video-related products. To expand our product offerings, in June 2004, we acquired the high-speed data equipment BAS division of ADC Telecommunications, Inc. Our principal executive offices are located at 475 Broadway Street, Redwood City, California 94063, and our telephone number is 650-995-5000. We operate research and development facilities in Westborough, Massachusetts, Tel Aviv, Israel and Redwood City, California. As of December 31, 2006, we had 562 employees. Except where the context requires otherwise, in this prospectus the "Company," "BigBand," "we," "us" and "our" refer to BigBand Networks, Inc., a Delaware corporation, and, where appropriate, its subsidiaries.

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Common stock offered by us 7,500,000 shares

Common stock offered by the selling stockholders 3,200,000 shares

Common stock to be outstanding after this offering 57,119,068 shares

Use of proceeds We intend to use the net proceeds to us from this offering for the repayment of approximately \$14.0 million in indebtedness, for working capital, for capital expenditures and for other general corporate purposes. We may also use a portion of our net proceeds to fund acquisitions of complementary businesses, products or technologies. We will not receive any of the proceeds from the sale of shares by the selling stockholders. See "Use of Proceeds."

NASDAQ Global Market symbol BBN1D

The number of shares of common stock that will be outstanding after this offering is based on the number of shares outstanding at December 31, 2006, which excludes:

- 16,019,932 shares of common stock issuable upon the exercise of options outstanding at December 31, 2006, at a weighted-average exercise price of \$2.31 per share;
- 933,670 shares of common stock issuable upon the exercise of warrants outstanding at December 31, 2006, at a weighted-average exercise price of \$3.63 per share, of which warrants to purchase 104,653 shares of common stock at a weighted-average exercise price of \$2.20 per share will expire at the closing of this offering if they have not been exercised;
- 1,000,000 shares of common stock reserved for future issuance under our Employee Stock Purchase Plan; and
- 6,000,000 shares of common stock reserved for future issuance under our 2007 Equity Incentive Plan, plus any shares reserved but not issued under our other stock option plans as of the date of this offering.

Unless otherwise indicated, all information in this prospectus assumes:

- the automatic conversion of all outstanding shares of our preferred stock into an aggregate of _____ shares of common stock effective immediately prior to the closing of this offering;
- a 1-for-4 reverse stock split effected in February 2007; and
- no exercise by the underwriters of their right to purchase up to 1,605,000 shares of common stock from the selling stockholders to cover over-allotments.

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We present below our summary consolidated financial information. The summary consolidated statements of operations data for the years ended December 31, 2004, 2005 and 2006 and the summary consolidated balance sheet data as of December 31, 2006 have been derived from audited consolidated financial statements included elsewhere in this prospectus. You should read this information together with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our audited consolidated financial statements and related notes, each included elsewhere in this prospectus. Our historical results are not necessarily indicative of the results to be expected in any future period.

	Years Ended December 31,		
	2004	2005	2006
	(in thousands, except per share data)		
Consolidated Statements of Operations Data⁽¹⁾:			
Net revenues			
Products	\$ 31,536	\$ 85,966	\$154,013
Services	<u>3,936</u>	<u>12,013</u>	<u>22,611</u>
Total net revenues	<u>35,472</u>	<u>97,979</u>	<u>176,624</u>
Cost of net revenues ⁽²⁾			
Products	21,300	55,933	74,152
Services	<u>2,221</u>	<u>3,900</u>	<u>9,245</u>
Total cost of net revenues	<u>23,521</u>	<u>59,833</u>	<u>83,397</u>
Gross profit			
Products	10,236	30,033	79,861
Services	<u>1,715</u>	<u>8,113</u>	<u>13,366</u>
Total gross profit	<u>11,951</u>	<u>38,146</u>	<u>93,227</u>
Operating expense			
Research and development ⁽²⁾	21,582	30,701	37,194
Sales and marketing ⁽²⁾	15,891	22,729	29,523
General and administrative ⁽²⁾	5,782	6,984	13,176
Amortization of purchased intangible assets	286	573	572
In-process research and development	<u>966</u>	<u>—</u>	<u>—</u>
Total operating expense	<u>44,507</u>	<u>60,987</u>	<u>80,465</u>
Operating income (loss)	(32,556)	(22,841)	12,762
Other income (expense), net	<u>(957)</u>	<u>(1,696)</u>	<u>(1,360)</u>
Net income (loss) before provision for income taxes and cumulative effect of change in accounting principle	<u>(33,513)</u>	<u>(24,537)</u>	<u>11,402</u>
Provision for income taxes	<u>250</u>	<u>325</u>	<u>2,525</u>
Net income (loss) before cumulative effect of change in accounting principle	<u>(33,763)</u>	<u>(24,862)</u>	<u>8,877</u>
Cumulative effect of change in accounting principle	<u>—</u>	<u>(633)</u>	<u>—</u>
Net income (loss)	<u><u>\$(33,763)</u></u>	<u><u>\$(25,495)</u></u>	<u><u>\$ 8,877</u></u>
Net income (loss) per common share:			
Basic	\$ (4.20)	\$ (2.36)	\$ 0.78
Diluted	<u>\$ (4.20)</u>	<u>\$ (2.36)</u>	<u>\$ 0.16</u>
Shares used in computing net income (loss) per common share:			
Basic	8,032	10,794	11,433
Diluted	<u>8,032</u>	<u>10,794</u>	<u>57,053</u>
Pro forma net income per common share: (unaudited)			
Basic			\$ 0.18
Diluted			<u>\$ 0.16</u>
Shares used in computing pro forma net income per common share: (unaudited) ⁽³⁾			
Basic			49,195
Diluted			<u>57,053</u>

(Footnotes appear on the next page)

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	As of December 31, 2006		
	Actual	Pro Forma ⁽⁴⁾ (in thousands)	Pro Forma As Adjusted ⁽⁵⁾
Consolidated Balance Sheet Data:			
Cash, cash equivalents and marketable securities	\$ 65,474	\$ 65,474	\$ 140,420
Working capital	25,056	28,208	109,610
Total assets	129,050	129,050	202,536
Current and long-term debt	14,536	14,536	536
Preferred stock warrant liabilities	3,152	—	—
Redeemable convertible preferred stock	117,307	—	—
Common stock and additional paid-in capital	17,075	137,534	225,809

- (1) On June 29, 2004, we completed the acquisition of Broadband Access Systems, Inc., which we refer to as BAS, from ADC Telecommunications, Inc. in a transaction accounted for as a business combination using the purchase method. For further information on the BAS acquisition, see Note 4 of the Notes to Consolidated Financial Statements included in this prospectus.
- (2) Includes stock-based compensation as follows

	Years Ended December 31,		
	2004	2005	2006
	(in thousands)		
Cost of net revenues	\$ 46	\$ 87	\$ 336
Research and development	299	516	1,035
Sales and marketing	134	263	637
General and administrative	222	237	516
Total stock-based compensation	<u>\$701</u>	<u>\$1,103</u>	<u>\$2,524</u>

- (3) The pro forma weighted average common shares outstanding reflects the conversion of our redeemable convertible preferred stock (using the if-converted method) into common stock as though the conversion had occurred on the original date of issuance.
- (4) The pro forma column in the summary consolidated balance sheet data table above gives effect to the conversion of all outstanding shares of our redeemable convertible preferred stock and all outstanding shares of non-voting class B common stock into common stock upon the completion of this offering, resulting in the termination of the redeemable convertible preferred stock and class B common stock conversion feature, the termination of the redemption rights associated with the class B common stock and the reclassification of the preferred stock warrant liabilities to additional paid-in capital upon closing of this offering.
- (5) The pro forma as adjusted column in the summary consolidated balance sheet data table above gives effect to items described in footnote (4) as well as our receipt of the estimated net proceeds from the sale of 7,500,000 shares of common stock offered by us in this offering, based on the initial public offering price of \$13.00 per share and after deducting estimated underwriting discounts and commissions and estimated offering expenses payable by us and our use of proceeds from this offering to repay approximately \$14.0 million of outstanding indebtedness.

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You should carefully consider the risks described below before making an investment decision. Our business, prospects, financial condition or operating results could be materially adversely affected by any of these risks, as well as other risks not currently known to us or that we currently consider immaterial. The trading price of our common stock could decline due to any of these risks, and you may lose all or part of your investment. In assessing the risks described below, you should also refer to the other information contained in this prospectus, including our consolidated financial statements and the related notes, before deciding to purchase any shares of our common stock.

Risks Related to our Business

We depend on the adoption of advanced technologies by cable operators and telephone companies for substantially all of our net revenues, and any decrease or delay in capital spending for these advanced technologies would harm our operating results, financial condition and cash flows.

Substantially all of our sales are dependent upon the adoption of advanced technologies by cable operators and telephone companies, and we expect these sales to continue to constitute a significant majority of our sales for the foreseeable future. Demand for our products will depend on the magnitude and timing of capital spending by service providers on advanced technologies for constructing and upgrading their network infrastructure, and a reduction or delay in this spending could have a material adverse effect on our business.

The capital spending patterns of our existing and potential customers are dependent on a variety of factors, including:

- available capital and access to financing;
- annual budget cycles;
- overall consumer demand for video, voice and data services and the acceptance of newly introduced services;
- competitive pressures, including pricing pressures;
- the impact of industry consolidation;
- the strategic focus of our customers and potential customers;
- technology adoption cycles and network architectures of service providers, and evolving industry standards that may impact them;
- the status of federal, local and foreign government regulation of telecommunications and television broadcasting, and regulatory approvals that our customers need to obtain;
- discretionary customer spending patterns;
- bankruptcies and financial restructurings within the industry; and
- general economic conditions

Any slowdown or delay in the capital spending by service providers as a result of any of the above factors would likely have a significant impact on our quarterly revenue and profitability levels.

Our operating results are likely to fluctuate significantly and may fail to meet or exceed the expectations of securities analysts or investors or our guidance, causing our stock price to decline.

Our operating results have fluctuated in the past and are likely to continue to fluctuate, on an annual and a quarterly basis, as a result of a number of factors, many of which are outside of our control. These factors include:

- the level and timing of capital spending of our customers, both in the United States and in international markets;
- the timing, mix and amount of orders, especially from significant customers;

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- changes in market demand for our products;
- our ability to secure significant orders from telephone companies;
- our mix of products sold between video products, which generally have higher margins, and our cable modem termination system, or CMTS, data products, which generally have lower margins;
- the mix of software and hardware products sold;
- our unpredictable and lengthy sales cycles, which typically range from nine to eighteen months;
- the timing of revenue recognition on sales arrangements, which may include multiple deliverables;
- new product introductions by our competitors;
- market acceptance of new or existing products offered by us or our customers;
- competitive market conditions, including pricing actions by our competitors;
- our ability to complete complex development of our software and hardware on a timely basis;
- our ability to design, install and receive customer acceptance of our products;
- unexpected changes in our operating expense;
- the potential loss of key manufacturer and supplier relationships;
- the cost and availability of components used in our products;
- changes in domestic and international regulatory environments; and
- the impact of new accounting rules.

We establish our expenditure levels for product development and other operating expense based on projected sales levels, and our expenses are relatively fixed in the short term. Accordingly, variations in the timing of our sales can cause significant fluctuations in operating results. As a result of all these factors, our operating results in one or more future periods may fail to meet or exceed the expectations of securities analysts or investors or our guidance, which would likely cause the trading price of our common stock to decline substantially.

We anticipate that our gross margins will fluctuate with changes in our product mix and expected decreases in the average selling prices of our products, which may adversely impact our operating results.

Our industry has historically experienced a decrease in average selling prices. We anticipate that the average selling prices of our products will decrease in the future in response to competitive pricing pressures, increased sales discounts and new product introductions by our competitors. We may experience substantial decreases in future operating results due to the decrease of our average selling prices. To maintain our gross margin levels, we must develop and introduce on a timely basis new products and product enhancements as well as continually reduce our product costs. Our failure to do so would likely cause our revenue and gross margins to decline, which could have a material adverse effect on our operating results and cause the price of our common stock to decline. We also anticipate that our gross margins will fluctuate from period to period as a result of the mix of products we sell in any given period, with our video products generally yielding higher gross margins than our data products. If our sales of these lower margin products significantly expand in future quarterly periods, our overall gross margin levels and operating results would be adversely impacted.

Our continued growth will depend significantly on our ability to deliver products that help enable telephone companies to provide video services. If the projected growth in demand for video services from telephone companies does not materialize or if these service providers find alternative methods of delivering video services, future sales of our video products will suffer.

Prior to 2006, our sales were principally to cable operators. In 2006, however, we generated significant sales from telephone companies. Our growth is dependent on our ability to sell video products to telephone companies that are increasingly reliant on the delivery of video services to their customers. Although a number of our

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existing products are being deployed in these networks, we will need to devote considerable resources to obtain orders, qualify our products and hire knowledgeable personnel to address telephone company customers, each of which will require significant time and financial commitment. These efforts may not be successful in the near future, or at all. If technological advancements allow these telephone companies to provide video services without upgrading their current system infrastructure or that allow them a more cost-effective method of delivering video services than our products, projected sales of our video products will suffer. Even if these providers choose our video products, they may not be successful in marketing video services to their customers, in which case additional sales of our products would likely be reduced.

Selling successfully to the telephone company market will be a significant challenge for us. Several of our largest competitors, such as Cisco Systems and Motorola Corporation, have mature customer relationships with many of the largest telephone companies, while we have limited recent experience with sales and marketing efforts designed to reach these potential customers. In addition, telephone companies face specific network architecture and legacy technology issues that we have only limited expertise in addressing. If we fail to penetrate the telephone company market successfully, our growth in revenues and operating results would be correspondingly limited.

Our customer base has become increasingly concentrated, and there are a limited number of potential customers for our products. The loss of any of our key customers would likely reduce our revenues significantly.

Historically, a large portion of our sales have been to a limited number of customers. Sales to our five largest customers accounted for approximately 90% of our net revenues in the three months ended December 31, 2006, approximately 79% of our net revenues in the year ended December 31, 2006, approximately 69% of our net revenues in the year ended December 31, 2005, and approximately 61% of our net revenues in the year ended December 31, 2004. In 2006, Comcast, Cox, Time Warner Cable and Verizon each represented 10% or more of our net revenues. In 2005, Adelphia, Cox and Time Warner Cable each represented 10% or more of our net revenues. In 2004, Adelphia, Comcast, Cox and Time Warner Cable each represented 10% or more of our net revenues.

We anticipate that a large portion of our revenues will continue to depend on sales to a limited number of customers, and we do not have contracts or other agreements that guarantee continued sales to these or any other customers. In addition, as the consolidation of ownership of cable operators and telephone companies continues, we may lose existing customers and have access to a shrinking pool of potential customers. We expect to see continuing industry consolidation and customer concentration due to the significant capital costs of constructing video, voice and data networks and for other reasons. For example, Adelphia, formerly the fifth largest cable company in the United States, which accounted for 5% of our net revenue in the year ended December 31, 2006, was sold in 2006 to Comcast and Time Warner Cable, the two largest U.S. cable operators. Further business combinations may occur in our customer base which will result in increased purchasing leverage by these customers over us. This may reduce the selling prices of our products and services and as a result may harm our business and financial results. Many of our customers desire to have two sources for the products we sell to them. As a result, our future revenue opportunities could be limited, and our profitability could be adversely impacted. The loss of, or reduction in orders from, any of our key customers would significantly reduce our revenues and have a material adverse impact on our business, operating results and financial condition.

The timing of a significant portion of our net revenues is dependent on complex systems integration.

We derive a significant portion of our net revenues from sales that include the network design, installation and integration of equipment, including equipment acquired from third parties to be integrated with our products to the specifications of our customers. We base our revenue forecasts on the estimated timing to complete the network design, installation and integration of our customer projects and customer acceptance of those products. The systems of our customers are both diverse and complex, and our ability to configure, test and integrate our systems with other elements of our customers' networks is dependent upon technologies provided to our

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customers by third parties. As a result, the timing of our revenue related to the implementation of our product applications in these complex networks is difficult to predict and could result in lower than expected revenue in any particular quarter. Similarly, our ability to deploy our equipment in a timely fashion can be subject to a number of other risks, including the availability of skilled engineering and technical personnel, the availability of equipment produced by third parties and our customers' need to obtain regulatory approvals.

If revenues forecasted for a particular period are not realized in such period due to the lengthy, complex and unpredictable sales cycles of our products, our operating results for that or subsequent periods will be harmed.

The sales cycles of our products are typically lengthy, complex and unpredictable and usually involve:

- a significant technical evaluation period;
- a significant commitment of capital and other resources by service providers;
- substantial time required to engineer the deployment of new technologies or new video, voice and data services;
- substantial testing and acceptance of new technologies that affect key operations; and
- substantial test marketing of new services with subscribers.

For these and other reasons, our sales cycles generally have been between nine and eighteen months, but can last longer. If orders forecasted for a specific customer for a particular quarter do not occur in that quarter, our operating results for that quarter could be substantially lower than anticipated. Our quarterly and annual results may fluctuate significantly due to revenue recognition policies and the timing of the receipt of orders.

We only recently became profitable, and we may not be able to sustain profitability in future periods.

The three-month periods ended September 30, 2006 and December 31, 2006 have been the only fiscal quarters in which we have achieved profitability. We were profitable for our 2006 fiscal year, however, we reported losses for our 2005 and 2004 fiscal years. We are continuing to incur increased research and development, sales and marketing, and general and administrative expenses. As a result, we may not be able to sustain profitability in future fiscal quarters or achieve profitability on an annual basis in the future.

Our independent registered public accountants have identified and reported to us material weaknesses in our internal controls for the years ended December 31, 2004 and 2005 that, if not properly remediated, could result in material misstatements in our financial statements in future periods and impair our ability to comply with the accounting and reporting requirements applicable to public companies.

In connection with the audits of our consolidated financial statements for each of the years ended December 31, 2004 and 2005, our independent registered public accounting firm identified material weaknesses in our internal control over financial reporting under the standards established by the American Institute of Certified Public Accountants. Our independent registered public accounting firm has indicated that the material weaknesses in our revenue recognition process and financial statement closing process resulted from having insufficient procedures in place and an insufficient number of qualified resources in our finance department with the required proficiency to apply our accounting policies in accordance with U.S. generally accepted accounting principles, or GAAP. Our independent registered public accounting firm was not, however, engaged to audit the effectiveness of our internal control over financial reporting. If such an evaluation had been performed or when we are required to perform such an evaluation, additional material weaknesses, significant deficiencies and other control deficiencies may have been or may be identified. Ensuring that we have adequate internal financial and accounting controls and procedures in place to help produce accurate financial statements on a timely basis is a costly and time-consuming effort that needs to be evaluated frequently, as described further under "We will incur increased costs and demands upon management as a result of complying with the laws and regulations affecting public companies, which could adversely affect our operating results."

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Because of these material weaknesses, there is heightened risk that a material misstatement of our annual or quarterly financial statements will not be prevented or detected. While we have completed our remediation efforts to address these material weaknesses, we cannot assure you that these remediation efforts have been entirely successful or that similar material weaknesses will not recur. Once we become a public company, we will be required to comply with the requirements of Section 404 of the Sarbanes-Oxley Act of 2002 as of December 31, 2008 and subsequent fiscal years. In the event that we have not adequately remedied these material weaknesses, and if we fail to maintain proper and effective internal controls in future periods, it could adversely affect our operating results, financial condition and our ability to run our business effectively and could cause investors to lose confidence in our financial reporting.

If we do not adequately manage and evolve our financial reporting and managerial systems and processes, our operating results and financial condition may be harmed.

Our ability to successfully implement our business plan and comply with regulations applicable to being a public reporting company requires an effective planning and management process. We expect that we will need to continue to improve existing, and implement new, operational and financial systems, procedures and controls to manage our business effectively in the future. Any delay in the implementation of, or disruption in the transition to, new or enhanced systems, procedures or controls, could harm our ability to accurately forecast sales demand, manage our supply chain and record and report financial and management information on a timely and accurate basis. In addition, the successful enhancement of our operational and financial systems, procedures and controls will result in higher general and administrative costs in future periods, and may adversely impact our operating results and financial condition.

In connection with our implementation, in the third quarter of 2006, of more stringent controls related to contracts for providing customer support, we discovered that certain end users in China maintained that they were entitled to company-provided support, while our contracts with these customers did not provide for customer support. In response, the Audit Committee of our Board of Directors conducted an independent investigation of the matter, employing independent counsel and an independent accounting firm. The investigation, which was completed in December 2006, found numerous instances in which resellers of our product applications in China, with the understanding and approval of our China personnel, agreed to provide technical support, extended warranty terms and potentially other undefined terms without proper documentation and without communicating these arrangements to our legal and finance departments. As a result, we have deferred approximately \$5.1 million in revenue as of December 31, 2006 from customers in China, which will be recognized in future periods if we satisfy all of the elements of our revenue recognition criteria. Our controls previously in place did not prevent these occurrences and we have therefore implemented a number of additional controls and remedial actions to ensure the appropriate accounting of future transactions and control over contracts with end users in China. In the event that we have not adequately implemented these additional controls and remedial actions, additional material weaknesses could be identified and could cause investors to lose confidence in our financial reporting.

We may not accurately anticipate the timing of the market needs for our products and develop such products at the appropriate times, which could harm our operating results and financial condition.

Accurately forecasting and meeting our customers' requirements is critical to the success of our business. Forecasting to meet customers' needs is particularly difficult in connection with newer products and products under development. Our ability to meet customer demand depends on our ability to configure our product applications to the complex architecture that our customers have developed, the availability of components and other materials and the ability of our contract manufacturers to scale their production of our products. Our ability to meet customer requirements depends on our ability to obtain sufficient volumes of these components and materials in a timely fashion. If we fail to meet customers' supply expectations, our net revenues will be adversely affected, and we will likely lose business. In addition, our priorities for future product development are based on our expectations of how the market for video, voice and data services will continue to develop in the United States and in international markets. If the market for such services develops more rapidly than we

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anticipate, then our product development efforts may be behind, which may result in our being unable to recoup our capital spent on product development as a result of a missed market opportunity. Conversely, if the market develops more slowly than we anticipate, we may find that we have expended significant capital on product development prior to our being able to generate any revenues for those products. If we are unable to accurately time our product introductions to meet market demand, it could have a material adverse impact on our operating results and financial condition.

In addition, if actual orders are materially lower than the indications we receive from our customers, our ability to manage inventory and expenses will also be harmed. If we enter into purchase commitments to acquire components and materials, or expend resources to manufacture products, and those products are not purchased by our customers when expected, our business and operating results could suffer.

We need to develop and introduce new and enhanced products in a timely manner to remain competitive, and our product development efforts require substantial research and development expense.

The markets in which we compete are characterized by continuing technological advancement, changes in customer requirements and evolving industry standards. To compete successfully, we must design, develop, manufacture and sell new or enhanced products that provide increasingly higher levels of performance and reliability and meet the cost expectations of our customers. Our product development efforts require substantial research and development expense. Research and development expense in the year ended December 31, 2006 was \$37.2 million, in the year ended December 31, 2005 was \$30.7 million and in the year ended December 31, 2004 was \$21.6 million. There can be no assurance that we will achieve an acceptable return on our research and development efforts.

We are currently developing a modular cable modem termination system, or M-CMTS, that we believe will be important for our future revenue growth and operating results. If we fail to deliver our M-CMTS product to market in a timely and cost-effective manner, or if our M-CMTS product fails to operate with all the functionality our customers expect, our future operating results would be harmed. Likewise, new technologies, standards and formats are being adopted by our customers. While we are in the process of developing products based on many of these new formats in order to remain competitive, we do not have such products at this time and cannot be certain when, if at all, we will have products in support of such new formats.

Our future growth depends on market acceptance of several emerging video, voice and data services, on the adoption of new network architectures and technologies and on several other industry trends.

Future demand for our products will depend significantly on the growing market acceptance of several emerging video, voice and data services, including high-speed data services; HDTV; addressable advertising; video delivered over telephone company networks; and VoIP.

The effective delivery of these services will depend on service providers developing and building new network architectures to deliver them. If the introduction or adoption of these services or the deployment of these networks is not as widespread or as rapid as we or our customers expect, our revenue growth will be limited.

Furthermore, we expect the extent and nature of regulatory attitudes towards issues such as competition among service providers, access by third parties to networks of other service providers and new services such as VoIP to impact our customers' purchasing decisions. If service providers do not pursue the opportunity to offer integrated video, voice and data services as aggressively as we expect, our revenue growth would be limited.

The markets in which we operate are intensely competitive, and many of our competitors are larger, more established and better capitalized than we are.

The markets for selling network-based hardware and software products to service providers are extremely competitive and have been characterized by rapid technological change. In the CMTS market, we compete

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principally with Cisco Systems, Motorola and Arris. In the video market, we compete broadly with system suppliers including Harmonic, Motorola, Scientific Atlanta (a division of Cisco Systems), SeaChange International, Tandberg Television (which recently announced that it will be acquired by Arris), Terayon Communication Systems and a number of smaller companies. We may not be able to compete successfully in the future, which may harm our business.

Many of our competitors are substantially larger and have greater financial, technical, marketing and other resources than us. Given their capital resources, many of these large organizations are in a better position to withstand any significant reduction in capital spending by customers in these markets. They often have broader product lines and market focus and are not as susceptible to downturns in a particular market. In addition, many of our competitors have been in operation much longer than we have and therefore have more long-standing and established relationships with domestic and foreign service providers. If any of our competitors' products or technologies were to become the industry standard, our business would also be seriously harmed. If our competitors are successful in bringing their products to market earlier, or if their products are more technologically capable than ours, then our sales could be materially adversely affected.

Recently, we have seen rapid consolidation among our competitors, such as Cisco's acquisition of Scientific Atlanta and purchases of VOD solutions by each of Cisco, Harmonic and Motorola. In addition, some of our competitors have entered into strategic relationships with one another to offer a more comprehensive solution than would be available individually. We expect this trend to continue as companies attempt to strengthen or maintain their market positions in the evolving industry for video. Many of the companies driving this consolidation trend have significantly greater financial, technical and other resources than we do, and are much better positioned than we are to offer complementary products and technologies. These combined companies may offer more compelling product offerings and be able to offer greater pricing flexibility, making it more difficult for us to compete while sustaining acceptable gross margins. Finally, continued industry consolidation may impact customers' perceptions of the viability of smaller companies, which may affect their willingness to purchase products from us. These competitive pressures could harm our business, operating results and financial condition.

In the event that certain of our competitors integrate products performing functions similar to our products into their existing network infrastructure offerings, our existing and potential customers may decide against using our products in their networks, which would harm our business.

Other providers of network-based hardware and software products are offering or announcing functionality aimed at solving similar problems addressed by our products. For example, several vendors have recently announced their intention to develop a switched broadcast product application. The inclusion of, or the announcement of the intent to include, functionality perceived to be similar to our product offerings in our competitors' products that have been accepted as necessary components of network architecture may have an adverse effect on our ability to market and sell our products. Furthermore, even if the functionality offered by other network infrastructure providers is more limited than our products, a significant number of customers may elect to accept such limited functionality in lieu of adding components from a different vendor. Many of our existing and potential customers have invested substantial personnel and financial resources to design and operate their networks and have mature relationships with other providers of network infrastructure products, which may make them reluctant to add new components to their networks, particularly from new vendors. In addition, our customers' other vendors with a broader product offering may be able to offer pricing or other concessions that we are not able to match because we currently offer a more modest suite of products and have fewer resources. If our existing or potential customers are reluctant to add network infrastructure from new vendors or otherwise decide to work with their existing vendors, our business, operating results and financial condition will be adversely affected.

We need to develop additional distribution channels to market and sell our products.

The majority of our sales to date have been direct sales to large cable operators in North America. Our video products have been traditionally sold to large cable operators with recent sales to telephone companies. We have

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not focused on smaller service providers and have had only limited access to service providers in certain international markets, including Asia and Europe. Although we intend to establish strategic relationships with leading distributors worldwide in an attempt to reach new customers, we may not succeed in establishing these relationships. Even if we do establish these relationships, the distributors may not succeed in marketing our products to their customers. Some of our competitors have established long-standing relationships with cable operators and telephone companies that may limit our and our distributors' ability to sell our products to those customers. Even if we were to sell our products to those customers, it would likely not be based on long-term commitments, and those customers would be able to terminate their relationships with us at any time without significant penalties.

We depend on a limited number of third parties to manufacture, assemble and supply our products.

We obtain many components and modules necessary for the manufacture or integration of our products from a sole supplier or a limited group of suppliers, with whom we do not generally maintain long-term agreements. Our reliance on sole or limited suppliers involves several risks, including the inability to obtain an adequate supply of required components or modules and reduced control over pricing, quality and timely delivery of components. For example, we depend exclusively on Broadcom for one of the chipsets in our CMTS product. Our ability to deliver our products on a timely basis to our customers would be materially adversely impacted if we needed to find alternative replacements for the chipsets, central processing units or power supplies that we use in our products. Significant time and effort would be required to locate new vendors for these alternative components, if alternatives are even available to us. In addition, the lead times associated with certain components are lengthy and preclude rapid changes in quantity requirements and delivery schedules.

In addition, increased demand by third parties for the components we use in our products may lead to decreased availability and higher prices for those components, since we carry little inventory of our products and product components. As a result, we may not be able to secure sufficient components at reasonable prices or of acceptable quality to build products in a timely manner, which would impact our ability to deliver products to our customers, and our business, operating results and financial condition would be adversely affected.

We currently rely on a single contract manufacturer, ACT Corporation, to assemble our products, manage our supply chain and negotiate component costs for our CMTS products. Likewise, we rely exclusively on Flextronics to assemble our products, manage our supply chain and negotiate component costs for our video products. Our reliance on these contract manufacturers reduces our control over the assembly process, exposing us to risks, including reduced control over quality assurance, production costs and product supply. If we fail to manage our relationships with these contract manufacturers effectively, or if these contract manufacturers experience delays, disruptions, capacity constraints or quality control problems in their operations, our ability to ship products to our customers could be impaired and our competitive position and reputation could be harmed. If contract manufacturers are unable to negotiate with their suppliers for reduced component costs, our operating results would be harmed. If we are required to change contract manufacturers, we may lose net revenues, incur increased costs and damage our customer relationships. Qualifying a new contract manufacturer and commencing volume production are expensive and time-consuming.

We must manage the expected growth in our business effectively even if our infrastructure, management and resources might be strained.

We have experienced rapid growth in our business in recent periods. This growth and any future growth will likely place a significant strain on our resources. For example, we are currently planning to hire additional development, sales, customer support, marketing and administrative personnel. In addition, we may need to expand and otherwise improve our internal systems, including our management information systems, customer relationship and support systems, and operating, administrative and financial systems and controls. This effort may require us to make significant capital expenditures or incur significant expenses, and divert the attention of management, sales, support and finance personnel from our core business operations, which may adversely affect our financial performance in future periods. Moreover, our growth has resulted, and any future growth will result,

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in increased responsibilities of management personnel. Managing this growth will require substantial resources that we may not have or otherwise be able to obtain.

Our products must interoperate with many software applications and hardware found in our customers' networks. If we are unable to ensure that our products interoperate properly, our business would be harmed.

Our products must interoperate with our customers' existing networks, which often have varied and complex specifications, utilize multiple protocol standards, software applications and products from multiple vendors, and contain multiple generations of products that have been added over time. As a result, we must continually ensure that our products interoperate properly with these existing networks. To meet these requirements, we must undertake development efforts that require substantial capital investment and the devotion of substantial employee resources. We may not accomplish these development efforts quickly or cost-effectively, if at all. For example, our products currently interoperate with set-top boxes marketed by vendors such as Scientific Atlanta and Motorola and with VOD servers marketed by SeaChange and C-COR. If we fail to maintain compatibility with these set-top boxes, VOD servers or other software or equipment found in our customers' existing networks, we may face substantially reduced demand for our products, which would adversely affect our business, operating results and financial condition.

We have entered into interoperability arrangements with a number of equipment and software vendors for the use or integration of their technology with our products. In these cases, the arrangements give us access to and enable interoperability with various products in the digital video market that we do not otherwise offer. If these relationships fail, we will have to devote substantially more resources to the development of alternative products and the support of our products, and our efforts may not be as effective as the combined solutions with our current partners. In many cases, these parties are either companies that we compete with directly in other areas, such as Motorola, or companies that have extensive relationships with our existing and potential customers and may have influence over the purchasing decisions of these customers. A number of our competitors have stronger relationships with some of our existing and potential partners and, as a result, our ability to have successful partnering arrangements with these companies may be harmed. Our failure to establish or maintain key relationships with third party equipment and software vendors may harm our ability to successfully sell and market our products. We are currently investing, and plan to continue to invest, significant resources to develop these relationships. Our operating results could be adversely affected if these efforts do not generate the revenues necessary to offset this investment.

In addition, if we find errors in the existing software or defects in the hardware used in our customers' networks or problematic network configurations or settings, as we have in the past, we may have to modify our software or hardware so that our products will interoperate with our customers' networks. This could cause longer installation times for our products and could cause order cancellations, either of which would adversely affect our business, operating results and financial condition.

Our failure to adequately protect our intellectual property and proprietary rights may adversely affect us.

We hold numerous issued U.S. patents and have a number of patent applications pending in the United States and foreign jurisdictions. Although we attempt to protect our intellectual property rights through patents, trademarks, copyrights, licensing arrangements, maintaining certain technology as trade secrets and other measures, we cannot assure you that any patent, trademark, copyright or other intellectual property rights owned by us will not be invalidated, circumvented or challenged, that such intellectual property rights will provide competitive advantages to us or that any of our pending or future patent applications will be issued with the scope of the claims sought by us, if at all. Despite our efforts, other competitors may be able to develop technologies that are similar or superior to our technology, duplicate our technology or design around the patents that we own. In addition, effective patent, copyright and trade secret protection may be unavailable or limited in certain foreign countries in which we do business or may do business in the future.

The steps that we have taken may not be able to prevent misappropriation of our technology. In addition, we may take legal action to enforce our patents and other intellectual property rights, protect our trade secrets.

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determine the validity and scope of the proprietary rights of others, or to defend against claims of infringement or invalidity. Such litigation could result in substantial costs and diversion of resources and could negatively affect our business, operating results and financial condition.

In order to successfully develop and market certain of our planned products, we may be required to enter into technology development or licensing agreements with third parties. Although companies may be willing to enter into technology development or licensing agreements, such agreements may not be negotiated on terms acceptable to us, or at all. Our failure to enter into technology development or licensing agreements, when necessary, could limit our ability to develop and market new products and could cause our business to suffer.

Our use of open source and third-party software could impose limitations on our ability to commercialize our products.

We incorporate open source software into our products, including certain open source code which is governed by the GNU General Public License, Lesser GNU General Public License and Common Development and Distribution License. The terms of many open source licenses have not been interpreted by U.S. courts, and there is a risk that these licenses could be construed in a manner that could impose unanticipated conditions or restrictions on our ability to commercialize our products. In such event, we could be required to seek licenses from third parties in order to continue offering our products, make generally available, in source code form, proprietary code that links to certain open source modules, re-engineer our products, discontinue the sale of our products if re-engineering could not be accomplished on a cost-effective and timely basis, or become subject to other consequences, any of which could adversely affect our business, operating results and financial condition.

We may also find that we need to incorporate certain proprietary third-party technologies, including software programs, into our products in the future. However, licenses to relevant third-party technology may not be available to us on commercially reasonable terms, if at all. Therefore, we could face delays in product releases until alternative technology can be identified, licensed or developed, and integrated into our current products. These delays, if they occur, could materially adversely affect our business, operating results and financial condition.

We may face intellectual property infringement claims from third parties.

Our industry is characterized by the existence of an extensive number of patents and frequent claims and related litigation regarding patent and other intellectual property rights. From time to time, third parties have asserted and may assert patent, copyright, trademark and other intellectual property rights against us or our customers. Our suppliers and customers may have similar claims asserted against them. We have agreed to indemnify some of our suppliers and customers for alleged patent infringement. The scope of this indemnity varies, but, in some instances, includes indemnification for damages and expenses including reasonable attorneys' fees. Any future litigation, regardless of its outcome, could result in substantial expense and significant diversion of the efforts of our management and technical personnel. An adverse determination in any such proceeding could subject us to significant liabilities, temporary or permanent injunctions or require us to seek licenses from third parties or pay royalties that may be substantial. Furthermore, necessary licenses may not be available on satisfactory terms, or at all.

Our business is subject to the risks of warranty returns, product liability and product defects.

Products like ours are very complex and can frequently contain undetected errors or failures, especially when first introduced or when new versions are released. Despite testing, errors may occur. Product errors could affect the performance of our products, delay the development or release of new products or new versions of products, adversely affect our reputation and our customers' willingness to buy products from us and adversely affect market acceptance or perception of our products. Any such errors or delays in releasing new products or new versions of products or allegations of unsatisfactory performance could cause us to lose revenue or market share, increase our service costs, cause us to incur substantial costs in redesigning the products, subject us to liability for damages and divert our resources from other tasks, any one of which could materially adversely

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affect our business, results of operations and financial condition. Our products must successfully interoperate with products from other vendors. As a result, when problems occur in a network, it may be difficult to identify the sources of these problems. The occurrence of hardware and software errors, whether or not caused by our products, could result in the delay or loss of market acceptance of our products, and therefore delay our ability to recognize revenue from sales, and any necessary revisions may cause us to incur significant expenses. The occurrence of any such problems could harm our business, operating results and financial condition.

Although we have limitation of liability provisions in our standard terms and conditions of sale, they may not fully or effectively protect us from claims as a result of federal, state or local laws or ordinances or unfavorable judicial decisions in the United States or other countries. The sale and support of our products also entails the risk of product liability claims. We maintain insurance to protect against certain claims associated with the use of our products, but our insurance coverage may not adequately cover any claim asserted against us. In addition, even claims that ultimately are unsuccessful could result in our expenditure of funds in litigation and divert management's time and other resources.

Our ability to sell our products is highly dependent on the quality of our support and services offerings, and our failure to offer high-quality support and services would have a material adverse effect on our sales and results of operations.

Once our products are deployed within our customers' networks, our customers depend on our support organization to resolve any issues relating to our products. If we or our channel partners do not effectively assist our customers in deploying our products, succeed in helping our customers quickly resolve post-deployment issues and provide effective ongoing support, our ability to sell our products to existing customers would be adversely affected and our reputation with potential customers could be harmed. In addition, as we expand our operations internationally, our support organization will face additional challenges including those associated with delivering support, training and documentation in languages other than English. Our failure to maintain high-quality support and services would have a material adverse effect on our business, operating results and financial condition.

Competition for qualified personnel, particularly management and research and development personnel, is intense. In order to manage our expected growth, we must be successful in attracting and retaining qualified personnel.

Our future success will depend on the ability of our management to operate effectively, both individually and as a group. We are dependent on our ability to retain and motivate high caliber personnel, in addition to attracting new personnel. The loss of any of our senior management or other key product development or sales and marketing personnel could adversely affect our future business, operating results and financial condition. In addition, a large number of our research and product development personnel have broad expertise in video algorithms, radio frequency and digital video standards that is vitally important in our product development efforts. If we were to lose a significant number of these research and development employees, our ability to develop successful new products would be harmed, and our revenues and operating results would likely suffer as a result. Competition for qualified management, technical and other personnel can be intense, and we may not be successful in attracting and retaining such personnel. While our employees are required to sign standard agreements concerning confidentiality and ownership of inventions, we generally do not have employment contracts or non-competition agreements with our personnel. The loss of the services of any of our key personnel, the inability to attract or retain qualified personnel in the future or delays in hiring required personnel, particularly senior management and engineers and other technical personnel, could negatively affect our business, operating results and financial condition.

Our further expansion into international markets may not succeed.

International sales represented \$19.2 million of our net revenues for the year ended December 31, 2006, \$16.8 million of our net revenues for the year ended December 31, 2005, and \$6.9 million of our net revenues for the year ended December 31, 2004. We intend to continue expanding into international markets. We are currently

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expanding our indirect sales channels in Europe and Asia through distributor and reseller arrangements with third parties. However, we may not be able to successfully enter into additional reseller and/or distribution agreements and/or may not be able to successfully manage our product sales channels. In addition, many of our resellers also sell products from other vendors that compete with our products and may choose to focus on products of those vendors. Additionally, our ability to utilize an indirect sales model in these international markets will depend on our ability to qualify and train those resellers to perform product installations and to provide customer support. If we fail to develop and cultivate relationships with significant resellers, or if these resellers are not successful in their sales efforts whether because they are unable to provide support or otherwise, we may be unable to grow or sustain our revenue in international markets.

Our continued growth will require further expansion of our international operations in Europe, Asia Pacific and other markets. We are presently establishing a small research and development presence in China. Managing research and development operations in numerous locations requires substantial management oversight. If we are unable to expand our international operations successfully and in a timely manner, our business, operating results and financial condition may be harmed. Such expansion may be more difficult or take longer than we anticipate, and we may not be able to successfully market, sell, deliver and support our products internationally.

Our international operations, the international operations of our contract manufacturers and our outsourced development contractors, and our efforts to increase sales in international markets, are subject to a number of risks, including:

- political and economic instability;
- unpredictable changes in foreign government regulations and telecommunications standards;
- legal and cultural differences in the conduct of business;
- import and export license requirements, tariffs, taxes and other trade barriers;
- inflation and fluctuations in currency exchange rates;
- difficulty in collecting accounts receivable;
- potentially adverse tax consequences;
- the burden of complying with a wide variety of foreign laws, treaties and technical standards;
- difficulty in protecting our intellectual property;
- acts of war or terrorism and insurrections;
- difficulty in staffing and managing foreign operations; and
- changes in economic policies by foreign governments.

The effects of any of the risks described above could reduce our future revenues from our international operations.

Regional instability in Israel may adversely affect business conditions and may disrupt our operations and negatively affect our operating results.

A substantial portion of our research and development operations and our contract manufacturing occurs in Israel. As of December 31, 2006, we had 176 full-time employees located in Israel. In addition, we have additional capabilities at this facility consisting of customer service, marketing and general and administrative employees. Accordingly, we are directly influenced by the political, economic and military conditions affecting Israel, and any major hostilities, such as the recent hostilities in Lebanon, involving Israel or the interruption or curtailment of trade between Israel and its trading partners could significantly harm our business. The September 2001 terrorist attacks, the ongoing U.S. war on terrorism and the terrorist attacks and hostilities within Israel have heightened the risks of conducting business in Israel. In addition, Israel and companies doing business with Israel

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have, in the past, been the subject of an economic boycott. Israel has also been and is subject to civil unrest and terrorist activity, with varying levels of severity, since September 2000. Security and political conditions may have an adverse impact on our business in the future. Hostilities involving Israel or the interruption or curtailment of trade between Israel and its trading partners could adversely affect our operations and make it more difficult for us to recruit qualified personnel in Israel.

In addition, most of our employees in Israel are obligated to perform annual reserve duty in the Israel Defense Forces and several were called for active military duty in connection with the hostilities in Lebanon in mid-2006. Should hostilities in the region escalate again, some of our employees would likely be called to active military duty, possibly resulting in interruptions in our sales and development efforts and other impacts on our business and operations which we cannot currently assess.

We may engage in future acquisitions that dilute the ownership interests of our stockholders, cause us to incur debt or assume contingent liabilities.

As part of our business strategy, from time to time, we review potential acquisitions of other businesses, and we expect to acquire businesses, products, or technologies in the future. In the event of any future acquisitions, we could:

- issue equity securities which would dilute current stockholders' percentage ownership;
- incur substantial debt;
- assume contingent liabilities; or
- expend significant cash.

These actions could harm our business, operating results and financial condition, or the price of our common stock. Moreover, even if we do obtain benefits from acquisitions in the form of increased sales and earnings, there may be a delay between the time when the expenses associated with an acquisition are incurred and the time when we recognize such benefits. This is particularly relevant in cases where it is necessary to integrate new types of technology into our existing portfolio and where new types of products may be targeted for potential customers with which we do not have pre-existing relationships. Acquisitions and investment activities also entail numerous risks, including:

- difficulties in the assimilation of acquired operations, technologies and/or products;
- unanticipated costs associated with the acquisition transaction;
- the diversion of management's attention from other business;
- adverse effects on existing business relationships with suppliers and customers;
- risks associated with entering markets in which we have no or limited prior experience;
- the potential loss of key employees of acquired businesses;
- difficulties in the assimilation of different corporate cultures and practices; and
- substantial charges for the amortization of certain purchased intangible assets, deferred stock compensation or similar items.

We may not be able to successfully integrate any businesses, products, technologies or personnel that we might acquire in the future, and our failure to do so could have a material adverse effect on our business, operating results and financial condition.

Table of Contents***We are subject to import/export controls that could subject us to liability or impair our ability to compete in international markets.***

Our products are subject to U.S. export controls and may be exported outside the United States only with the required level of export license or through an export license exception, in most cases because we incorporate encryption technology into our products. In addition, various countries regulate the import of certain encryption technology and have enacted laws that could limit our ability to distribute our products or could limit our customers' ability to implement our products in those countries. Changes in our products or changes in export and import regulations may create delays in the introduction of our products in international markets, prevent our customers with international operations from deploying our products throughout their global systems or, in some cases, prevent the export or import of our products to certain countries altogether. Any change in export or import regulations or related legislation, shift in approach to the enforcement or scope of existing regulations, or change in the countries, persons or technologies targeted by such regulations, could result in decreased use of our products by, or in our decreased ability to export or sell our products to, existing or potential customers internationally.

In addition, we may be subject to customs duties and export quotas, which could have a significant impact on our revenue and profitability. While we have not encountered significant difficulties in connection with the sales of our products in international markets, the future imposition of significant increases in the level of customs duties or export quotas could have a material adverse effect on our business.

If we fail to comply with environmental regulatory requirements, our future revenues could be adversely affected.

We face increasing complexity in our product design and procurement operations as we adjust to new and upcoming requirements relating to the materials composition of many of our products. The European Union, or EU, has adopted certain directives to facilitate the recycling of electrical and electronic equipment sold in the EU, including the Restriction on the Use of Certain Hazardous Substances in Electrical and Electronic Equipment directive that restricts the use of lead, mercury and certain other substances in electrical and electronic products placed on the market in the EU after July 1, 2006. In connection with our compliance with these environmental laws and regulations, we have incurred substantial costs, including research and development costs, and costs associated with assuring the supply of compliant components from our suppliers. Similar laws and regulations have been proposed or may be enacted in other regions, including in the United States, China and Japan. Other environmental regulations may require us to reengineer our products to utilize components that are compatible with these regulations, and this reengineering and component substitution may result in additional costs to us or disrupt our operations or logistics.

New privacy laws and regulations or changing interpretations of existing laws and regulations could harm our business.

Governments in the United States and other countries have adopted laws and regulations regarding privacy and advertising that could impact important aspects of our business. In particular, governments are considering new limitations or requirements with respect to our customers' collection, use, storage and disclosure of personal information for marketing purposes. Any legislation enacted or regulation issued could dampen the growth and acceptance of addressable advertising which is enabled by our products. If the use of our products to increase advertising revenue is limited or becomes unlawful, our business, results of operations and financial condition would be harmed.

Recent accounting regulations related to equity compensation could adversely affect our earnings and our ability to attract and retain key personnel.

Since our inception, we have used stock options as a fundamental component of our employee compensation packages. We believe that our stock option plans are an essential tool to link the long-term interests of our stockholders and employees and serve to motivate management to make decisions that will, in the long run, give the best returns to stockholders. The Financial Accounting Standards Board has instituted changes

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to GAAP that require us to record a charge to earnings for employee stock option grants and employee stock purchase plan rights. In addition, NASDAQ Global Market, or NASDAQ, regulations requiring stockholder approval for all stock option plans could make it more difficult for us to grant options to employees in the future. To the extent that these or other new regulations make it more difficult or expensive to grant options to employees, we may incur increased compensation costs, change our equity compensation strategy or find it difficult to attract, retain and motivate employees, each of which could materially and adversely affect our business, operating results and financial condition.

Our business is subject to the risks of earthquakes, fire, floods and other natural catastrophic events, and to interruption by manmade problems such as computer viruses or terrorism.

Our corporate headquarters are located in the San Francisco Bay area, a region known for seismic activity. A significant natural disaster, such as an earthquake, fire or a flood, could have a material adverse impact on our business, operating results and financial condition. In addition, our servers are vulnerable to computer viruses, break-ins and similar disruptions from unauthorized tampering with our computer systems. In addition, acts of terrorism or war could cause disruptions in our or our customers' business or the economy as a whole. To the extent that such disruptions result in delays or cancellations of customer orders, or the deployment of our products, our business, operating results and financial condition would be adversely affected.

Risks Related to this Offering and Ownership of our Common Stock

We will incur increased costs and demands upon management as a result of complying with the laws and regulations affecting public companies, which could adversely affect our operating results.

As a public company we will incur significant legal, accounting and other expenses that we did not incur as a private company, including costs associated with public company reporting requirements. We also have incurred and will incur costs associated with recently adopted corporate governance requirements, including requirements under Section 404 and other provisions of the Sarbanes-Oxley Act, as well as rules implemented by the Securities and Exchange Commission, or SEC, and the NASDAQ. In addition, our management team will also have to adapt to the requirements of being a public company. The expenses incurred by public companies for reporting and corporate governance purposes have been increasing. We expect these rules and regulations to substantially increase our legal and financial compliance costs and to make some activities more time-consuming and costly. We are unable to currently estimate these costs with any degree of certainty. We also expect these new rules and regulations may make it more difficult and more expensive for us to obtain director and officer liability insurance, and we may be required to accept reduced policy limits and coverage or incur substantially higher costs to obtain the same or similar coverage than used to be available. As a result, it may be more difficult for us to attract and retain qualified individuals to serve on our board of directors or as our executive officers.

Our failure to raise additional capital or generate the significant capital necessary to expand our operations and invest in new products could reduce our ability to compete and could harm our business.

We expect that our existing cash and cash equivalents and existing amounts available under our revolving credit facility, together with the net proceeds from this offering, will be sufficient to meet our anticipated cash needs for at least the next twelve months. After that, we may need to raise additional funds, and we may not be able to obtain additional debt or equity financing on favorable terms, if at all. If we raise additional equity financing, our stockholders may experience significant dilution of their ownership interests and the per share value of our common stock could decline. If we engage in debt financing, we may be required to accept terms that restrict our ability to incur additional indebtedness and force us to maintain specified liquidity or other ratios, any of which could harm our business, operating results and financial condition. If we need additional capital and cannot raise it on acceptable terms, we may not be able to, among other things:

- develop or enhance our products and services;
- continue to expand our product development sales and marketing organizations;

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- acquire complementary technologies, products or businesses;
- expand operations, in the United States or internationally;
- hire, train and retain employees; or
- respond to competitive pressures or unanticipated working capital requirements.

Our failure to do any of these things could seriously harm our business, operating results and financial condition.

An active, liquid and orderly trading market for our common stock may not develop, the price of our stock may be volatile, and you could lose all or part of your investment.

Prior to this offering, there has been no public market for shares of our common stock. The initial public offering price of our common stock will be determined through negotiation with the underwriters. This price will not necessarily reflect the price at which investors in the market will be willing to buy and sell our shares of common stock following this offering. In addition, the trading price of our common stock following this offering is likely to be highly volatile and could be subject to wide fluctuations in response to various factors, some of which are beyond our control, including those factors described above in “Our operating results are likely to fluctuate significantly and may fail to meet or exceed the expectations of securities analysts or investors or our guidance, causing our stock price to decline.”

In addition, the stock market in general, and the market for technology companies in particular, has experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of those companies. Broad market and industry factors may seriously affect the market price of companies’ stock, including ours, regardless of actual operating performance. These fluctuations may be even more pronounced in the trading market for our stock shortly following this offering. In addition, in the past, following periods of volatility in the overall market and the market price of a particular company’s securities, securities class action litigation has often been instituted against these companies. This litigation, if instituted against us, could result in substantial costs and a diversion of our management’s attention and resources.

Concentration of ownership among our existing executive officers, directors and their affiliates may prevent new investors from influencing significant corporate decisions.

Upon completion of this offering, our executive officers, directors and their affiliates will beneficially own, in the aggregate, approximately 53% of our outstanding common stock. As a result, these stockholders will be able to exercise a significant level of control over all matters requiring stockholder approval, including the election of directors, amendment of our certificate of incorporation and approval of significant corporate transactions. This control could have the effect of delaying or preventing a change of control of our company or changes in management and will make the approval of certain transactions difficult or impossible without the support of these stockholders. See “Principal and Selling Stockholders” for additional detail about the shareholdings of these persons.

Future sales of shares by existing stockholders could cause our stock price to decline.

If our existing stockholders sell, or indicate an intention to sell, substantial amounts of our common stock in the public market after the lock-up and other legal restrictions on resale discussed in this prospectus lapse, the trading price of our common stock could decline. Based on shares of common stock outstanding as of December 31, 2006, upon completion of this offering, we will have outstanding a total of 57,119,068 shares of common stock. Of these shares, only the 10,700,000 shares of common stock sold in this offering by us and the selling stockholders will be freely tradable, without restriction, in the public market. Our underwriters, however, may, in their sole discretion, permit our officers, directors and other current stockholders who are subject to the contractual lock-up to sell shares prior to the expiration of the lock-up agreements.

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We expect that the lock-up agreements pertaining to this offering will expire 180 days from the date of this prospectus (subject to extension upon the occurrence of specified events). After the lock-up agreements expire, up to an additional 46,343,200 shares of common stock will be eligible for sale in the public market, 32,235,089 of which shares are held by directors, executive officers and other affiliates and will be subject to volume limitations under Rule 144 under the Securities Act and various vesting agreements. In addition, shares of common stock that are either subject to outstanding options or reserved for future issuance under our employee benefit plans will become eligible for sale in the public market to the extent permitted by the provisions of various vesting agreements, the lock-up agreements and Rule 144 and Rule 701 under the Securities Act. If these additional shares of common stock are sold, or if it is perceived that they will be sold, in the public market, the trading price of our common stock could decline.

Anti-takeover provisions contained in our certificate of incorporation and bylaws, as well as provisions of Delaware law, could impair a takeover attempt.

Our certificate of incorporation, bylaws and Delaware law contain provisions which could have the effect of rendering more difficult or discouraging an acquisition deemed undesirable by our board of directors. Our corporate governance documents include provisions:

- creating a classified board of directors whose members serve staggered three-year terms;
- authorizing blank check preferred stock, which could be issued with voting, liquidation, dividend and other rights superior to our common stock;
- limiting the liability of, and providing indemnification to, our directors and officers;
- limiting the ability of our stockholders to call and bring business before special meetings;
- requiring advance notice of stockholder proposals for business to be conducted at meetings of our stockholders and for nominations of candidates for election to our board of directors;
- controlling the procedures for the conduct and scheduling of board and stockholder meetings; and
- providing the board of directors with the express power to postpone previously scheduled annual meetings and to cancel previously scheduled special meetings.

These provisions, alone or together, could delay hostile takeovers and changes in control or changes in our management.

As a Delaware corporation, we are also subject to provisions of Delaware law including Section 203 of the Delaware General Corporation law, which prevents some stockholders holding more than 15% of our outstanding common stock from engaging in certain business combinations without approval of the holders of substantially all of our outstanding common stock.

Any provision of our certificate of incorporation or bylaws, or Delaware law that has the effect of delaying or deterring a change in control could limit the opportunity for our stockholders to receive a premium for their shares of our common stock, and could also affect the price that some investors are willing to pay for our common stock.

Purchasers in this offering will experience immediate and substantial dilution in the book value of their investment.

The initial public offering price of our common stock is substantially higher than the net tangible book value per share of our outstanding common stock immediately after this offering. Therefore, if you purchase our common stock in this offering, you will incur an immediate dilution of \$11.07 in net tangible book value per share from the price you paid. In addition, following this offering, purchasers in the offering will have contributed 43.1% of the total consideration paid by our stockholders to purchase shares of common stock. The exercise of outstanding options and warrants will result in further dilution. For a further description of the dilution that you will experience immediately after this offering, see "Dilution."

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Our management will have broad discretion over the use of the proceeds we receive in this offering and might not apply the proceeds in ways that increase the value of your investment.

Our management will have broad discretion to use our net proceeds from this offering, and you will be relying on the judgment of our management regarding the application of these proceeds. Our management might not apply our net proceeds of this offering in ways that increase the value of your investment. We expect to use the net proceeds from this offering for the repayment of certain outstanding indebtedness and for general corporate purposes, including working capital and capital expenditures, which may in the future include investments in, or acquisitions of, complementary businesses, services or technologies. Our management might not be able to yield a significant return, if any, on any investment of these net proceeds. You will not have the opportunity to influence our decisions on how to use our net proceeds from this offering.

Table of Contents**SPECIAL NOTE REGARDING FORWARD LOOKING STATEMENTS AND INDUSTRY DATA**

This prospectus includes forward looking statements. All statements other than statements of historical facts contained in this prospectus, including statements regarding our future results of operations and financial position, business strategy and plans and our objectives for future operations, are forward-looking statements. The words "believe," "may," "will," "estimate," "continue," "anticipate," "intend," "expect" and similar expressions are intended to identify forward looking statements. We have based these forward looking statements largely on our current expectations and projections about future events and financial trends that we believe may affect our financial condition, results of operations, business strategy, short term and long term business operations and objectives, and financial needs. These forward looking statements are subject to a number of risks, uncertainties and assumptions, including those described in "Risk Factors." In light of these risks, uncertainties and assumptions, the forward looking events and circumstances discussed in this prospectus may not occur and actual results could differ materially and adversely from those anticipated or implied in the forward looking statements.

Moreover, we operate in a very competitive and rapidly changing environment. New risks emerge from time to time. It is not possible for our management to predict all risks, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. Before investing in our common stock, investors should be aware that the occurrence of the risks, uncertainties and events described in the section entitled "Risk Factors" and elsewhere in this prospectus could have a material adverse effect on our business, results of operations and financial condition.

You should not rely upon forward-looking statements as predictions of future events. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee that the future results, levels of activity, performance or events and circumstances reflected in the forward-looking statements will be achieved or occur. Moreover, neither we nor any other person assumes responsibility for the accuracy and completeness of the forward-looking statements. We undertake no obligation to update publicly any forward-looking statements for any reason after the date of this prospectus to conform these statements to actual results or to changes in our expectations.

This prospectus also contains statistical data and estimates, including those relating to market size and growth rates of the markets in which we participate, that we obtained from industry publications and reports generated by American Advertising Federation, In-Stat, IDC, Kagan Research LLC, Yankee Group Research Inc. and ZenithOptimedia Group. These publications typically indicate that they have obtained their information from sources they believe to be reliable, but do not guarantee the accuracy and completeness of their information. Although we have assessed the information in the publications and found it to be reasonable and believe the publications are reliable, we have not independently verified their data.

You should read this prospectus and the documents that we reference in this prospectus and have filed with the SEC as exhibits to the registration statement of which this prospectus is a part with the understanding that our actual future results, levels of activity, performance and events and circumstances may be materially different from what we expect.

Table of Contents**USE OF PROCEEDS**

We estimate that our net proceeds from the sale of the common stock that we are offering will be approximately \$88.3 million, based upon an initial public offering price of \$13.00 per share, after deducting underwriting discounts and commissions and estimated offering expenses that we must pay. We will not receive any proceeds from the sale of shares of common stock by the selling stockholders.

We expect to use a portion of our net proceeds to repay the entire outstanding balance under our term loan and revolving credit facility with Silicon Valley Bank, which was approximately \$14.0 million as of December 31, 2006. This term loan bears interest at the Federal Reserve's prime rate plus 0.25%, which was 8.50% as of December 31, 2006, and this revolving credit facility bears interest at the Federal Reserve's prime rate, which was 8.25% as of December 31, 2006. The term loan has a maturity date of August 18, 2009. The revolving credit facility has a maturity date of August 18, 2008. We have used the proceeds of the term loan and the revolving credit facility for working capital and other general corporate purposes.

We intend to use the remaining net proceeds to us from this offering for working capital, capital expenditures and other general corporate purposes. We may also use a portion of our net proceeds to fund acquisitions of complementary businesses, products or technologies. However, we do not have agreements or commitments for any specific repayments or acquisitions at this time.

Pending use of the proceeds as described above, we intend to invest the proceeds in short-term, interest-bearing, investment-grade securities.

DIVIDEND POLICY

We have never declared or paid cash dividends on our common or preferred stock. We currently do not anticipate paying any cash dividends in the foreseeable future. Any future determination to declare cash dividends will be made at the discretion of our board of directors, subject to applicable laws and compliance with certain covenants under our credit facility, which restrict or limit our ability to pay dividends, and will depend on our financial condition, results of operations, capital requirements, general business conditions and other factors that our board of directors may deem relevant.

Table of Contents**CAPITALIZATION**

The following table sets forth our capitalization as of December 31, 2006:

- on an actual basis;
- on a pro forma basis to give effect to the conversion of all outstanding shares of our redeemable convertible preferred stock and all outstanding shares of non-voting class B common stock into common stock upon the completion of this offering, resulting in the termination of the redeemable convertible preferred stock and class B common stock conversion feature, the termination of the redemption rights associated with the class B common stock and the reclassification of the preferred stock warrant liabilities to additional paid-in capital upon closing of this offering; and
- on a pro forma as adjusted basis to reflect, in addition, our receipt of the estimated net proceeds from the sale of 7,500,000 shares of common stock offered by us in this offering, based on the initial public offering price of \$13.00 per share, after deducting underwriting discounts and commissions and estimated offering expenses payable by us, our use of proceeds from this offering to repay approximately \$14.0 million of outstanding indebtedness and the filing of the restated certificate of incorporation upon completion of this offering.

You should read this table together with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements and related notes included elsewhere in this prospectus.

	As of December 31, 2006		
	Actual	Pro Forma	Pro Forma As Adjusted
	(in thousands, except per share data)		
Cash, cash equivalents and marketable securities	\$ 65,474	\$ 65,474	\$ 140,420
Current and long-term debt	14,536	14,536	536
Preferred stock warrant liability	3,152	—	—
Redeemable convertible preferred stock: \$0.01 par value; 128,266 shares authorized and 29,439 shares issued and outstanding actual; no shares authorized and no shares issued and outstanding pro forma; 5,000 shares authorized and no shares issued and outstanding pro forma as adjusted	117,307	—	—
Common stock, \$0.001 par value; 335,000 shares authorized actual; 335,000 shares authorized pro forma; 250,000 shares authorized pro forma as adjusted			
Class A voting: 300,000 shares designated and 8,241 shares issued and outstanding actual; 300,000 shares designated and 49,619 shares issued and outstanding pro forma; 250,000 shares designated and 57,119 shares issued and outstanding pro forma as adjusted	8	50	57
Class B non-voting: 35,000 shares designated and 3,619 shares issued and outstanding actual; no shares designated and no shares issued and outstanding pro forma; no shares designated and no shares issued and outstanding pro forma as adjusted	4	—	—
Additional paid-in capital	17,063	137,484	225,752
Deferred stock-based compensation	(1,405)	(1,405)	(1,405)
Accumulated other comprehensive income	9	9	9
Accumulated deficit	(111,293)	(111,293)	(111,293)
Total stockholders' equity (deficit)	(95,614)	24,845	113,120
Total capitalization	\$ 39,381	\$ 39,381	\$ 113,656

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This table excludes the following shares:

- 16,019,932 shares of common stock issuable upon exercise of stock options as of December 31, 2006, at a weighted-average exercise price of \$2.31 per share;
- 933,670 shares of common stock issuable upon exercise of warrants outstanding as December 31, 2006, at a weighted-average exercise price of \$3.63 per share, of which warrants to purchase 104,653 shares of common stock at a weighted-average exercise price of \$2.20 per share will expire at the closing of this offering if they have not been exercised;
- 1,000,000 shares of common stock reserved for future issuance under our Employee Stock Purchase Plan; and
- 6,000,000 shares of common stock reserved for future issuance under our 2007 Equity Incentive Plan, plus any shares reserved but not issued under our other stock option plans as of the date of this offering.

Table of Contents**DILUTION**

Our pro forma net tangible book value as of December 31, 2006, was \$21.9 million, or \$0.44 per share of common stock. Net tangible book value per share represents the amount of stockholders' equity divided by 49,619,068 shares of common stock outstanding after giving effect of the automatic conversion of all outstanding shares of preferred stock into shares of common stock and all of the outstanding class B common stock into shares of common stock, and the reclassification of the preferred stock warrant liabilities to additional paid-in capital each upon the closing of this offering.

Net tangible book value dilution per share to new investors represents the difference between the amount per share paid by purchasers of shares of common stock in this offering and the pro forma net tangible book value per share of common stock immediately after the completion of this offering. After giving effect to our sale of 7,500,000 shares of common stock in this offering at the initial public offering price of \$13.00 per share, and after deducting the underwriting discounts and commissions and estimated offering expenses payable by us, our pro forma net tangible book value as of December 31, 2006 would have been, \$110.2 million, or \$1.93 per share. This represents an immediate increase in net tangible book value of \$1.49 per share to existing stockholders and an immediate dilution in net tangible book value of \$11.07 per share to investors purchasing common stock in this offering, as illustrated in the following table:

Initial public offering price per share	\$13.00
Pro forma net tangible book value per share as of December 31, 2006, before giving effect to this offering	\$0.44
Increase in pro forma net tangible book value per share attributed to new investors purchasing shares in this offering	<u>1.49</u>
Pro forma net tangible book value per share after giving effect to this offering	<u>1.93</u>
Dilution per share to new investors in this offering	<u>\$11.07</u>

The following table presents on a pro forma basis as of December 31, 2006, after giving effect to the sale of 7,500,000 shares and the automatic conversion of all preferred stock into common stock upon completion of this offering, the differences between the existing stockholders and the purchasers of shares in this offering with respect to the number of shares purchased from us, the total consideration paid and the average price paid per share:

	Shares Purchased		Total Consideration		Average Price Per Share
	Number	Percent	Amount	Percent	
	(in thousands, except per share data and percent)				
Existing stockholders	49,619	86.9%	\$128,571	56.9%	\$ 2.59
New public investors	<u>7,500</u>	<u>13.1</u>	<u>97,500</u>	<u>43.1</u>	13.00
Total	<u>57,119</u>	<u>100.0%</u>	<u>\$226,071</u>	<u>100.0%</u>	

The above discussion and table assume no exercise of stock options or warrants outstanding as of December 31, 2006, including 16,019,932 shares of common stock issuable upon exercise of options with a weighted-average exercise price of \$2.31 per share and 933,670 shares of common stock issuable upon exercise of warrants with a weighted-average exercise price of \$3.63 per share. If all of these options and warrants were exercised, then our existing stockholders, including the holders of these options and warrants, would own 89.9% and our new investors would own 10.1% of the total number of shares of our common stock outstanding upon the closing of this offering.

Table of Contents**SELECTED CONSOLIDATED FINANCIAL DATA**

The following selected consolidated financial data should be read in conjunction with the section titled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the consolidated financial statements and the related notes included in this prospectus. The selected consolidated financial data included in this section is not intended to replace the consolidated financial statements and the related notes included in this prospectus.

The consolidated statements of operations data for the years ended December 31, 2004, 2005 and 2006, and consolidated balance sheets data as of December 31, 2005 and 2006, were derived from our audited consolidated financial statements that are included elsewhere in this prospectus. The consolidated statements of operations data for the years ended December 31, 2002 and 2003, and consolidated balance sheets data as of December 31, 2002, 2003 and 2004, were derived from our audited consolidated financial statements not included in this prospectus. The historical results presented below are not necessarily indicative of financial results to be achieved in future periods.

	Years Ended December 31,				
	2002	2003	2004	2005	2006 ⁽⁴⁾
	(in thousands, except per share data)				
Consolidated Statements of Operations Data⁽¹⁾:					
Net revenues					
Products	\$ 9,203	\$ 20,014	\$ 31,536	\$ 85,966	\$154,013
Services	371	1,566	3,936	12,013	22,611
Total net revenues	9,574	21,580	35,472	97,979	176,624
Cost of net revenues ⁽²⁾					
Products	4,545	8,597	21,300	55,933	74,152
Services	213	1,027	2,221	3,900	9,245
Total cost of net revenues	4,758	9,624	23,521	59,833	83,397
Gross profit					
Products	4,658	11,417	10,236	30,033	79,861
Services	158	539	1,715	8,113	13,366
Total gross profit	4,816	11,956	11,951	38,146	93,227
Operating expenses					
Research and development ⁽²⁾	7,669	9,519	21,582	30,701	37,194
Sales and marketing ⁽²⁾	6,278	10,376	15,891	22,729	29,523
General and administrative ⁽²⁾	2,378	3,095	5,782	6,984	13,176
Amortization of purchased intangible assets	—	—	286	573	572
In-process research and development	—	—	966	—	—
Total operating expenses	16,325	22,990	44,507	60,987	80,465
Operating income (loss)	(11,509)	(11,034)	(32,556)	(22,841)	12,762
Other income (expense), net	(36)	(673)	(957)	(1,696)	(1,360)
Net income (loss) before provision for income taxes and cumulative effect of change in accounting principle	(11,545)	(11,707)	(33,513)	(24,537)	11,402
Provision for income taxes	—	—	250	325	2,525
Net income (loss) before cumulative effect of change in accounting principle	(11,545)	(11,707)	(33,763)	(24,862)	8,877
Cumulative effect of change in accounting principle	—	—	—	(633)	—
Net income (loss)	<u>\$(11,545)</u>	<u>\$(11,707)</u>	<u>\$(33,763)</u>	<u>\$(25,495)</u>	<u>\$ 8,877</u>
Net income (loss) per common share:					
Basic	<u>\$ (2.24)</u>	<u>\$ (2.01)</u>	<u>\$ (4.20)</u>	<u>\$ (2.36)</u>	<u>\$ 0.78</u>
Diluted	<u>\$ (2.24)</u>	<u>\$ (2.01)</u>	<u>\$ (4.20)</u>	<u>\$ (2.36)</u>	<u>\$ 0.16</u>
Shares used in computing net income (loss) per common share:					
Basic	5,159	5,832	8,032	10,794	11,433
Diluted	5,159	5,832	8,032	10,794	57,053
Pro forma net income per common share: (unaudited)					
Basic					\$ 0.18
Diluted					\$ 0.16
Shares used in computing pro forma net income per common share: (unaudited) ⁽³⁾					
Basic					49,195
Diluted					57,053

(Footnotes appear on the next page)

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	As of December 31,				
	2002	2003	2004 (in thousands)	2005	2006
Consolidated Balance Sheets Data:					
Cash, cash equivalents and marketable securities	\$ 9,638	\$ 14,290	\$ 23,796	\$ 24,287	\$ 65,474
Working capital	9,424	16,188	27,606	5,812	25,056
Total assets	21,920	30,862	80,052	76,816	129,050
Current and long-term debt	917	4,662	12,094	11,418	14,536
Preferred stock warrant liabilities ⁽⁵⁾	—	—	—	1,642	3,152
Redeemable convertible preferred stock	59,846	75,060	118,204	117,307	117,307
Common stock and additional paid-in capital	1,376	1,535	14,049	14,990	17,075
Total stockholders' deficit	\$(47,943)	\$(59,388)	\$(83,926)	\$(107,819)	\$(95,614)

- (1) On June 29, 2004, we completed the acquisition of Broadband Access Systems, Inc., which we refer to as BAS, from ADC Telecommunications, Inc. in a transaction accounted for as a business combination using the purchase method. For further information on our acquisition of BAS, see Note 4 of the Notes to Consolidated Financial Statements included in this prospectus.
- (2) Includes stock-based compensation as follows:

	Years Ended December 31,				
	2002	2003	2004 (in thousands)	2005	2006 ⁽⁴⁾
Cost of net revenues	\$ —	\$ —	\$ 46	\$ 87	\$ 336
Research and development	165	52	299	516	1,035
Sales and marketing	164	51	134	263	637
General and administrative	—	—	222	237	516
Total stock-based compensation	<u>\$329</u>	<u>\$ 103</u>	<u>\$ 701</u>	<u>\$1,103</u>	<u>\$ 2,524</u>

- (3) The pro forma weighted average common shares outstanding reflects the conversion of our redeemable convertible preferred stock (using the if-converted method) into common stock as though the conversion had occurred on the original date of issuance.
- (4) We adopted the fair value recognition and measurement provisions of SFAS No. 123R, *Share-Based Payments*, effective January 1, 2006, using the prospective transition method. For periods prior to January 1, 2006, we followed the intrinsic value recognition and measurement provisions of Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees*. For further information, see Note 2 to the Notes to Consolidated Financial Statements included in this prospectus.
- (5) We adopted the provisions of Financial Accounting Standards Board Staff Position No. 150-5, *Issuer's Accounting under Statement No. 150 for Freestanding Warrants and Other Similar Instruments on Shares that Are Redeemable*, or FSP 150-5, an interpretation of FASB Statement No. 150, *Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity*, effective July 1, 2005. Pursuant to FSP 150-5, freestanding warrants for shares that are either puttable or warrants for shares that are redeemable are classified as liabilities on the consolidated balance sheet at fair value. At the end of each reporting period, changes in fair value during the period are recorded as a component of other income (expense), net. Prior to July 1, 2005, we accounted for warrants for the purchase of preferred stock under EITF 96-18, *Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services*. For further information regarding the cumulative effect of accounting change from the adoption of FSP 150-5, see Note 2 of the Notes to Consolidated Financial Statements included in this prospectus.

Table of Contents**MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
AND RESULTS OF OPERATIONS**

The following discussion of our financial condition and results of operations should be read together with the consolidated financial statements and related notes that are included elsewhere in this prospectus. This discussion contains forward-looking statements, which are based upon current expectations that involve risks and uncertainties. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of various factors, including those set forth under "Risk Factors" or in other parts of this prospectus.

Overview

Our company was founded in December 1998, and through 2001 we were engaged principally in research and development. We first generated meaningful product revenues in 2002, principally from our initial media processing platform designed for video. Since 2003, we have expanded our customer base to include six of the ten largest service providers in the United States, including Cablevision, Comcast, Charter, Cox, Time Warner Cable and Verizon. To expand the breadth of our products, in June 2004, we acquired the high-speed data equipment BAS division of ADC Telecommunications, Inc. From 2003 through 2005, we experienced significant revenue growth that was derived primarily from cable operators. Beginning in 2005, we commenced sales efforts to telephone companies and began recognizing significant revenues from one of these companies in 2006.

We have been profitable on a quarterly basis since the three months ended September 30, 2006, and we first achieved profitability on an annual basis in 2006. As of December 31, 2006, we had an accumulated deficit of \$111.3 million.

Our net revenues are influenced by a variety of factors, including the level and timing of capital spending of our customers, and the annual budgetary cycles of, and the timing and amount of orders from, significant customers. The selling prices of our products vary based upon the particular customer implementation, which impacts the relative mix of software, hardware and services associated with the sale.

Our sales cycle for an initial customer purchase typically ranges from nine to eighteen months, but can be longer. This process generally involves several stages before we can recognize revenues on the sale of our products. As a provider of advanced technologies, we seek to actively participate with our existing and potential customers in the evaluation of their technology needs and network architectures, including the development of initial designs and prototypes. Following these activities, we typically respond to a service provider's request for proposal, configure our products to work within our customer's network architecture, and test our products first in laboratory testing and then in field environments to ensure interoperability with existing products in the service provider's network. Following testing, our revenue recognition depends on satisfying complex customer acceptance criteria specified in our contract with the customer and our customer's schedule for roll-out of the product. Completion of several of these stages is substantially outside of our control, which causes our revenue patterns from a given customer to vary widely from period to period. After initial deployment of our products, subsequent purchases of our products typically have a more compressed sales cycle.

Due to the nature of the cable and telecommunications industries, we sell our products to a limited number of large customers, which have varied over time. For the quarter ended December 31, 2006 and the years ended December 31, 2006, 2005 and 2004, we derived approximately 90%, 79%, 69% and 61% of our net revenues from our top five customers, respectively. In 2006, Comcast, Cox, Time Warner Cable and Verizon each represented 10% or more of our net revenues. In 2005, Adelphia, Cox and Time Warner Cable each represented 10% or more of our net revenues. In 2004, Adelphia, Comcast, Cox and Time Warner Cable each represented 10% or more of our net revenues. We believe that for the foreseeable future our net revenues will be highly concentrated in a relatively small number of large customers. The loss of one or more of our large customers, or the cancellation or deferral of purchases by one or more of these customers, would have a material adverse impact on our revenues and operating results.

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We sell our products and services to customers in the United States through our direct sales force. We sell to customers internationally through a combination of direct sales and resellers. In the year ended December 31, 2006, approximately 89% of our sales were to customers in the United States and 11% were to customers outside the United States. Domestic sales for 2005 and 2004 accounted for 83% and 80% of our total sales, respectively, while sales to customers outside of the United States accounted for 17% and 20% of our total sales, respectively.

Net Revenues. We derive our net revenues from sales of, and services for, video and data products. Our product revenues are comprised of a combination of software licenses and hardware. Our primary video products include Digital Simulcast, TelcoTV and Switched Broadcast. Our data products include High-Speed Data and Voice-over-IP. Our services include ongoing customer support and maintenance, product installation and training. Our customer support and maintenance is available in a tiered offering at either a standard or enhanced level. The substantial majority of our customers have purchased our enhanced level of customer support and maintenance. The accounting for our net revenues is complex and, as discussed below, we account for revenues in accordance with Statement of Position, or SOP 97-2, *Software Revenue Recognition*.

Cost of Net Revenues. Our cost of product revenues consists primarily of payments for components and product assembly, costs of product testing, provisions taken for excess and obsolete inventory and for warranty obligations and manufacturing overhead. Cost of services revenues is primarily comprised of personnel costs in providing technical support, costs incurred to support deployment and installation within our customers' networks and training costs.

Gross Margin. Our gross profit as a percentage of net revenues, or gross margin, has been and will continue to be affected by a variety of factors, including the mix of software and hardware sold, the mix of revenue between our video and data products, the average selling prices of our products, and the mix of revenue between products and services. We achieve a higher gross margin on the software content of our products compared to the hardware content. We also generally earn a higher gross margin on our video products compared to our data products. In general, we expect the average selling prices of our products to decline over time, but we seek to maintain our overall gross margins by introducing new products with higher margins, selling software enhancements to existing products, achieving price reductions for components and improving product design to reduce costs. Our gross margins for products are also influenced by the specific terms of our contracts, which may vary significantly from customer to customer based on the type of products sold, the overall size of the customer's order, and the architecture of the customer network, which can influence the amount and complexity of design, integration and installation services.

Operating Expense. Our operating expense consists of research and development, sales and marketing, general and administrative, in-process research and development and amortization of intangible assets. Personnel related costs are the most significant component of operating expense. We grew from 156 employees at December 31, 2003, to 562 at December 31, 2006. We expect to continue to hire a significant number of new employees to support the growth we anticipate.

Research and development expense is the largest component of our operating expense and consists primarily of personnel costs, independent contractor costs, prototype expenses and other allocated facilities and information technology expense. The majority of our research and development staff is focused on software development. All research and development costs are expensed as incurred. Our development teams are located in Westborough, Massachusetts, Tel Aviv, Israel and Redwood City, California. We expect our research and development expenses to continue to increase in absolute dollars in future periods.

Sales and marketing expense relates primarily to compensation and associated costs for marketing and sales personnel, sales commissions, promotional and other marketing expenses, travel, trade-show expenses, depreciation expenses for demonstration equipment used for trade-shows and allocated facilities and information technology expense. Marketing programs are intended to generate net revenues from new and existing customers and are expensed as incurred. We expect sales and marketing expense to increase in absolute dollars as we hire additional personnel, expand our sales and marketing efforts domestically and internationally and seek to increase our brand awareness.

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General and administrative expense consists primarily of compensation and associated costs for general and administrative personnel, professional fees and allocated facilities and information technology expenses. Professional services consist of outside legal, accounting and information technology and other consulting costs. We expect that general and administrative expense will increase in absolute dollars as we hire additional personnel, incur costs related to the anticipated growth of our business, and make improvements to our information technology infrastructure. In addition, we expect to incur significant additional costs as we transition to being a public company, including the costs of SEC reporting, Sarbanes-Oxley Act compliance and director and officer liability insurance.

BAS Acquisition

In June 2004, we acquired the BAS division of ADC Telecommunications, Inc. to expand our suite of product offerings with a high-speed data product. The aggregate consideration for this acquisition was valued at approximately \$25.1 million and was allocated between net tangible and intangible assets of \$19.8 million and \$5.3 million, respectively. The net tangible assets included a \$4.7 million increase in the basis of acquired inventory, all of which was sold by the end of 2005.

Critical Accounting Policies and Estimates

Our consolidated financial statements have been prepared in accordance with GAAP. The preparation of our consolidated financial statements requires our management to make estimates, assumptions, and judgments that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the applicable periods. Management bases its estimates, assumptions, and judgments on historical experience and on various other factors that are believed to be reasonable under the circumstances. Different assumptions and judgments would change the estimates used in the preparation of our consolidated financial statements, which, in turn, could change the results from those reported. Our management evaluates its estimates, assumptions and judgments on an ongoing basis.

The critical accounting policies requiring estimates, assumptions, and judgments that we believe have the most significant impact on our consolidated financial statements are described below.

Revenue Recognition

We derive net revenues from sales of our products and services. Product revenues consists of sales of our hardware and software products. Shipping charges, which have been insignificant to date, are included in product revenues, and the related shipping costs are included in cost of product revenue. Service revenues consists of customer support and maintenance, product installation and training activities.

Software is essential to the functionality of our products. We provide software updates that we choose to develop, which we refer to as unspecified software updates, and enhancements related to our products through support service contracts. As a result, we account for revenue in accordance with Statement of Position, or SOP 97-2, *Software Revenue Recognition as amended by SOP 98-9, Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions*, for all transactions involving the sale of software.

We recognize product revenue when all of the following have occurred: (1) we have entered into an arrangement with a customer; (2) delivery has occurred; (3) customer payment is deemed fixed or determinable and free of contingencies and significant uncertainties; and (4) collection is probable. Pricing is considered fixed or determinable at the execution of a customer arrangement, based on specific products and quantities to be delivered at specified prices. We assess the ability to collect from our customers based on a number of factors, including credit-worthiness and any past transaction history of the customer. In the limited circumstances where we may have a customer not deemed creditworthy, we will defer all net revenues from the arrangement until payment is received and all other revenue recognition criteria have been met.

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Product revenues consist of hardware and a perpetual license to our software. Product revenues are generally recognized upon transfer of title to the customer assuming all other revenue recognition criteria are met, except for customers that require contractually negotiated acceptance of our products, in which case we recognize net revenues at the earlier of receipt of acceptance from the customer or when the rejection period lapses. Substantially all of our contracts, including those with resellers, do not include rights of return. To the extent that our agreements contain such terms, we recognize revenue when the amount of future returns can be reasonably estimated in accordance with the guidance under Statement of Financial Accounting Standards No. 48 (as amended), *Revenue Recognition When Right of Return Exists*. Returns to date have been insignificant. Our resellers generally do not maintain any inventory and only receive products from us when an end-user customer has committed to the purchase.

Most of our products are sold in combination with customer support and maintenance services, which consist of software updates and product support. Software updates provide customers with rights to unspecified software updates that we choose to develop and to maintenance releases and patches released during the term of the support period. Product support services include telephone support, access to on-site technical support personnel and repair or replacement of hardware in the event of damage or failure during the term of the support period. Net revenues for support services are recognized on a straight-line basis over the service contract term, which is generally one year. Installation services and training services, when provided, are also recognized in service revenues when performed.

We use the residual method, as allowed by SOP 98-9, *Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions*, to recognize revenue when a customer arrangement includes one or more elements to be delivered at a future date and vendor specific objective evidence, or VSOE, of the fair value of all undelivered elements exists. Under the residual method, the fair value of the undelivered elements is deferred and any remaining amount provided for under the contract is recognized. When the undelivered element is customer support and maintenance, that portion of the revenue is recognized ratably over the term of the customer support arrangement, and the remaining revenue associated with the arrangement is recognized when all the other criteria of SOP 97-2 are satisfied. We have established VSOE of the fair value of our customer support and maintenance and other services based upon the normal pricing and discounting practices for those services when sold separately and the prices at which our customers have renewed their customer support and maintenance arrangements. If evidence of the fair value of one or more undelivered elements does not exist, all revenues are deferred and recognized when delivery of those elements occurs or when fair value can be established. For example, in situations where we sell a product which includes a commitment for delivery of a future specified software feature or functionality, we defer revenue recognition for the entire arrangement until the specified software feature or functionality is delivered.

Revenue recognition requirements under SOP 97-2 are very complex. In applying our revenue recognition policy, we must determine which portions of our revenue are recognized currently and which portions must be deferred.

Valuation of Inventories

Inventories are stated at the lower of cost or market. Cost is determined on the first-in, first-out method. We provide for excess and obsolete inventories after evaluation of historical sales and usage, current economic trends, market conditions, product rationalization, forecasted sales, product lifecycle and current inventory levels. Provisions for excess and obsolete inventory are recorded as cost of net product revenues. This evaluation requires us to make estimates regarding future events in an industry where rapid technological changes are prevalent. It is possible that increases in inventory write-downs may be required in the future if there is a decline in market conditions or if changes in expected product lifecycles occur. If market conditions improve or product lifecycles extend, we may have greater success in selling inventory that had previously been written down. In either event, the actual value of our inventory may be higher or lower and recognition of such difference will affect our cost of net revenues in a future period, which could materially affect our operating results and financial position.

Table of Contents**Warranty Liabilities**

We warrant our products against defects in materials and workmanship. Generally, we warrant our products for one year. For our largest telephone company customer, we warrant our products for five years. A provision for estimated future costs related to warranty activities is recorded as a component of cost of net product revenues when the product revenues are recognized based upon our historical product failure rates and historical costs incurred in correcting product failures. The recorded amount is adjusted from time to time for specifically identified warranty exposures. Where we have experienced higher product failure rates and costs of correcting product failures change, or our estimates relating to specifically identified warranty exposures changed, we have recorded additional warranty reserves and may be required to do so in future periods. If our estimated reserves differ from our actual warranty costs based on historical experience, we may reverse a portion of or increase such provisions in future periods. In the event we change our warranty reserve estimates, the resulting charge against future cost of sales or reversal of previously recorded charges may materially affect our gross margins and operating results.

Stock-Based Compensation

Prior to January 1, 2006, we accounted for employee stock options using the intrinsic value method in accordance with Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees*, or APB No. 25, and Financial Accounting Standards Board Interpretation No. 44, *Accounting for Certain Transactions Involving Stock Compensation, an Interpretation of APB No. 25*. The intrinsic value represents the difference between the per share market price of the stock on the date of grant and the per share exercise price of the respective stock option. The resulting stock-based compensation is deferred and amortized to expense over the grant's vesting period, which is generally four years.

During the year ended December 31, 2005, we granted options to employees to purchase a total of 1,883,437 shares of common stock at exercise prices ranging from \$1.00 to \$1.88 per share.

We estimated the market value of our common stock with the assistance of Empire Valuation Consultants, LLC, an unrelated third-party valuation firm. This firm provided contemporaneous valuation reports dated June 30, 2004, December 31, 2005, June 1, 2006, September 30, 2006, November 30, 2006 and December 31, 2006, which valued our common stock at \$1.68, \$2.20, \$2.56, \$5.28, \$5.36 and \$5.76, respectively.

We determined that the deemed market value of our common stock in 2005 ranged from \$1.68 to \$2.20 per share.

During 2006, we amortized \$1.1 million of deferred stock based compensation, leaving approximately \$1.4 million to be amortized in future periods. The total unamortized deferred stock-based compensation recorded for all outstanding option grants made through December 31, 2005 is expected to be amortized as follows: \$0.9 million in 2007, \$0.4 million in 2008 and \$22,000 in 2009.

On January 1, 2006, we adopted the provisions of the Financial Accounting Standards Board, or FASB, SFAS 123R, *Share-Based Payments*, or SFAS 123R. Under SFAS 123R, stock-based compensation costs for employees is measured at the grant date, based on the estimated fair value of the award at that date, and is recognized as expense over the employee's requisite service period, which is generally over the vesting period, on a straight-line basis. We adopted the provisions of SFAS 123R using the prospective transition method. Under this transition method, non-vested option awards outstanding at January 1, 2006, continue to be accounted for under the intrinsic value method under APB No. 25. All awards granted, modified or settled after the date of adoption are accounted for using the measurement, recognition and attribution provisions of SFAS 123R.

During the year ended December 31, 2006, we granted options to employees to purchase a total of 6,283,264 shares of common stock at exercise prices ranging from \$1.88 to \$5.36 per share. The deemed market value of our common stock on the dates these options were granted ranged from \$2.20 to \$5.60 per share.

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Information on employee stock options granted during the year ended December 31, 2006 is summarized as follows:

<u>Date of Issuance</u>	<u>Number of Options Granted</u>	<u>Exercise Price</u>	<u>Deemed Market Value</u>	<u>Intrinsic Value</u>
January 16, 2006	50,000	\$ 1.88	\$ 2.20	\$ 0.32
January 24, 2006	154,526	1.88	2.20	0.32
April 4, 2006	101,250	2.20	2.44	0.24
April 10, 2006	996,926	2.20	2.44	0.24
May 2, 2006	150,232	2.20	2.52	0.32
July 12, 2006	332,363	2.60	3.52	0.92
August 14, 2006	62,500	2.60	4.24	1.64
November 1, 2006	2,973,367	5.28	5.32	0.04
November 2, 2006	567,500	5.28	5.32	0.04
November 8, 2006	62,500	5.28	5.32	0.04
November 17, 2006	425,000	5.28	5.36	0.08
December 15, 2006	352,100	5.36	5.56	0.20
December 20, 2006	55,000	5.36	5.60	0.24

We make a number of estimates and assumptions related to SFAS 123R. The estimation of stock awards that will ultimately vest requires judgment, and to the extent actual results differ from our estimates, such amounts will be recorded as an adjustment in the period estimates are revised. Actual results may differ substantially from these estimates. In valuing share-based awards under SFAS 123R, significant judgment is required in determining the expected volatility of our common stock and the expected term individuals will hold their share-based awards prior to exercising. Expected volatility of the stock is based on our peer group in the industry in which we do business because we do not have sufficient historical volatility data for our own stock. The expected term of options granted represents the period of time that options granted are expected to be outstanding and was calculated using the simplified method permitted by the SEC Staff Accounting Bulletin No. 107. In the future, as we gain historical data for volatility in our own stock and the actual term employees hold our options, expected volatility and expected term may change which could substantially change the grant-date fair value of future awards of stock options and ultimately the expense we record.

As of December 31, 2006, the total compensation cost related to stock-based awards granted under SFAS 123R to employees and directors but not yet amortized was approximately \$19.1 million, net of estimated forfeitures. These costs, adjusted for changes in estimated forfeiture rates from time to time, will be amortized over the next four years. Amortization for the year ended December 31, 2006 was approximately \$1.4 million.

Allowances for Doubtful Accounts

We make judgments as to our ability to collect outstanding accounts receivable and provide allowances for the applicable portion of accounts receivable when collection becomes doubtful. We provide allowances based upon a specific review of all significant outstanding invoices, analysis of our historical collection experience and current economic trends. If the historical data we use to calculate the allowance for doubtful accounts does not reflect our future ability to collect outstanding accounts receivable, additional provisions for doubtful accounts may be needed and our future results of operations could be materially affected. Our allowance for doubtful accounts was approximately \$23,000 and \$152,000 at December 31, 2005 and 2006, respectively.

Estimation of Fair Value of Warrants to Purchase Redeemable Convertible Preferred Stock

On July 1, 2005, we adopted FSP 150-5. Our outstanding warrants to purchase shares of our redeemable convertible preferred stock are subject to the requirements in FSP 150-5, which require us to classify these warrants as current liabilities and to adjust the value of these warrants to their fair value at the end of each

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reporting period. At the time of adoption, we recorded \$0.6 million for the cumulative effect of this change in accounting principle to reflect the cumulative change in estimated fair value of these warrants as of that date. We recorded \$0.1 million and \$1.5 million of expense in other expense, net, for the remainder of 2005 and for the year ended December 31, 2006, respectively, to reflect further increases in the estimated fair value of the warrants. We estimated the fair value of these warrants at the respective balance sheet dates using the Black-Scholes option valuation model, based on the estimated market value of the underlying redeemable convertible preferred stock at the valuation measurement date, the remaining contractual term of the warrant, risk-free interest rates and expected dividends on and expected volatility of the price of the underlying redeemable convertible preferred stock. These estimates, especially the market value of the underlying redeemable convertible preferred stock and the expected volatility, are highly judgmental and could differ materially in the future.

Upon the closing of this offering, all outstanding warrants to purchase shares of series E-1 preferred stock and certain outstanding warrants to purchase series C preferred stock will become warrants to purchase shares of our common stock and, as a result, will no longer be subject to FSP 150-5. The then-current aggregate fair value of these warrants will be reclassified from liabilities to additional paid-in capital, a component of stockholder's equity, and we will cease to record any related periodic fair value adjustments. All outstanding warrants to purchase series A-1 preferred stock and certain outstanding warrants to purchase series C preferred stock will expire upon completion of the initial public offering if not previously exercised. We anticipate that we will incur a non-cash charge relating to our outstanding warrants for preferred stock in the quarter ending March 31, 2007. Assuming that the price at which our common stock is valued for these purposes is the initial public offering price of \$13.00 per share, the amount of that charge would be approximately \$3.0 million. The exact amount of the charge may depend on the closing trading price of our common stock on the NASDAQ Global Market on March 20, 2007, the expected date of the closing of this offering.

Impairment of Intangible Assets and Other Long-lived Assets

We assess impairment of long-lived assets in accordance with FAS No. 144, *Impairment of Long-Lived Assets* and test long-lived assets for recoverability when events or changes in circumstances indicate that their carrying amount may not be recoverable. Circumstances which could trigger a review include, but are not limited to: significant decreases in the market price of the asset; significant adverse changes in the business climate or legal factors; accumulation of costs significantly in excess of the amount originally expected for the acquisition or construction of the asset; current period cash flow or operating losses combined with a history of losses or a forecast of continuing losses associated with the use of the asset; or current expectation that the asset will more likely than not be sold or disposed of significantly before the end of its estimated useful life.

Recoverability is assessed based on the sum of the undiscounted cash flows expected to result from the use and the eventual disposal of the asset. An impairment loss is recognized in the consolidated statements of operations when the carrying amount is not recoverable and exceeds fair value, which is determined on a discounted cash flow basis.

We make estimates and judgments about future undiscounted cash flows and fair value. Although our cash flow forecasts are based on assumptions that are consistent with our plans, there is significant exercise of judgment involved in determining the cash flows attributable to a long-lived asset over its estimated remaining useful life. Our estimates of anticipated future cash flows could be reduced significantly in the future. As a result, the carrying amount of our long-lived assets could be reduced through impairment charges in the future. Changes in estimated future cash flows could also result in a shortening of estimated useful life of long-lived assets including intangibles for depreciation and amortization purposes.

Accounting for Income Taxes

As part of the process of preparing our consolidated financial statements we are required to estimate our taxes in each of the jurisdictions in which we operate. We estimate actual current tax exposure together with assessing temporary differences resulting from differing treatment of items, such as accruals and allowances not

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currently deductible for tax purposes. These differences result in deferred tax assets and liabilities, which are included in our consolidated balance sheets. In general, deferred tax assets represent future tax benefits to be received when certain expenses previously recognized in our consolidated statements of operations become deductible expenses under applicable income tax laws or loss or credit carry forwards are utilized. Accordingly, realization of our deferred tax assets is dependent on future taxable income against which these deductions, losses and credits can be utilized.

We must assess the likelihood that our deferred tax assets will be recovered from future taxable income and to the extent we believe that recovery is not likely, we must establish a valuation allowance.

Management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against our net deferred tax assets. As of December 31, 2006, we recorded a full valuation allowance against our deferred tax assets arising from U.S. operations since, based on the available evidence, we believed at that time it was more likely than not that we would not be able to utilize all of these deferred tax assets in the future. We intend to maintain the full valuation allowances until sufficient evidence exists to support the reversal of the valuation allowances. We make estimates and judgments about our future taxable income that are based on assumptions that are consistent with our plans and estimates. Should the actual amounts differ from our estimates, the amount of our valuation allowance could be materially impacted.

Revenue Recognition on Sales in China

In connection with our implementation, in the third quarter of 2006, of more stringent controls related to contracts for providing customer support, we discovered that certain end users in China maintained that they were entitled to company-provided support while our contracts with these customers did not provide for customer support. In response, the Audit Committee of our Board of Directors conducted an independent investigation of the matter, employing independent counsel and an independent accounting firm. The investigation, which was completed in December 2006, found numerous instances in which resellers of our products in China, with the understanding and approval of our China personnel, agreed to provide technical support, extended warranty terms and potentially other undefined terms without proper documentation and without communicating these arrangements to our legal and finance departments. As a result, we have deferred approximately \$5.1 million in revenue as of December 31, 2006 from customers in China, which will be recognized in future periods upon the satisfaction of all of the elements of our revenue recognition criteria. Our controls previously in place did not prevent these occurrences and we have therefore implemented a number of additional controls and remedial actions to ensure the appropriate accounting of future transactions and control over contracts with end users in China.

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The following table shows the percentage relationships of the listed items from our consolidated statements of operations, as a percentage of total net revenues for the periods indicated:

	Years Ended December 31,		
	2004	2005 (in percent)	2006
Consolidated Statements of Operations Data:			
Net revenues			
Products	88.9%	87.7%	87.2%
Services	<u>11.1</u>	<u>12.3</u>	<u>12.8</u>
Total net revenues	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>
Cost of net revenues			
Products	60.0	57.1	42.0
Services	<u>6.3</u>	<u>4.0</u>	<u>5.2</u>
Total cost of net revenues	<u>66.3</u>	<u>61.1</u>	<u>47.2</u>
Gross profit			
Products	28.9	30.6	45.2
Services	<u>4.8</u>	<u>8.3</u>	<u>7.6</u>
Total gross profit	<u>33.7</u>	<u>38.9</u>	<u>52.8</u>
Operating expense			
Research and development	60.8	31.3	21.1
Sales and marketing	44.8	23.2	16.7
General and administrative	16.4	7.1	7.5
Amortization of intangible assets	0.8	0.6	0.3
In-process research and development	<u>2.7</u>	<u>—</u>	<u>—</u>
Total operating expense	<u>125.5</u>	<u>62.2</u>	<u>45.6</u>
Operating income (loss)	(91.8)	(23.3)	7.2
Other expense, net	<u>(2.7)</u>	<u>(1.8)</u>	<u>(0.8)</u>
Net income (loss) before provision for income taxes and cumulative effect of change in accounting principle	(94.5)	(25.1)	6.4
Provision for income taxes	<u>0.7</u>	<u>0.3</u>	<u>1.4</u>
Net income (loss) before cumulative effect of change in accounting principle	(95.2)	(25.4)	5.0
Cumulative effect of change in accounting principle	<u>—</u>	<u>0.7</u>	<u>—</u>
Net income (loss)	<u>(95.2)%</u>	<u>(26.0)%</u>	<u>5.0%</u>

Years Ended December 31, 2006 and 2005

Net Revenues. Net revenues for 2006 were \$176.6 million compared to \$98.0 million for 2005, an increase of \$78.6 million, or 80.3%. Revenues from our top five customers comprised 79% and 69% of net revenues for 2006 and 2005, respectively. During 2006, revenues from customers in the United States comprised 89% of net revenues, and revenues from customers outside the United States comprised 11% of net revenues, compared to the same period in 2005, in which customers in the United States comprised 83% of net revenues, and revenues from customers outside the United States comprised 17% of net revenues.

Products revenues for 2006 were \$154.0 million compared to \$86.0 million for 2005, an increase of \$68.0 million, or 79.2%. This increase was primarily due to a \$87.6 million increase in revenues from our video products, partially offset by a \$19.6 million decrease in revenues from our data products. The \$87.6 million increase in video products was attributable to the first recognition of significant net revenues from our TelcoTV product and significant growth in revenues from our Switched Broadcast product. The decrease in revenues from data products was almost entirely due to \$18.8 million of revenues recognized in 2005 following satisfaction of customer acceptance criteria for product shipped to a single customer in 2004.

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Services revenues for 2006 was \$22.6 million compared to \$12.0 million for 2005, an increase of \$10.6 million, or 88.2%. This \$10.6 million increase was primarily due to an increase in customer support and maintenance revenues earned on a larger installed base of products.

Gross Profit/Gross Margin. Gross profit for 2006 was \$93.2 million compared to \$38.1 million for 2005, an increase of \$55.1 million, or 144.4%. Gross margin increased to 52.8% in 2006 compared to 38.9% in 2005.

Products gross margin for 2006 was 51.9% compared to 34.9% for 2005. This increase was due to a shift in product mix in 2006 towards video products, which have relatively higher gross margins. Gross margin in 2005 was adversely impacted by the sale of inventory acquired in the BAS transaction. Under purchase accounting, the carrying value of this inventory was increased by \$4.7 million to its fair market value at the time of acquisition. The sale of a portion of this inventory reduced products gross margin by \$3.5 million, or 4.1% of products revenues, in 2005. In addition, gross margins in 2005 decreased as a result of a physical inventory write-down of \$1.8 million and a specific warranty provision of \$1.5 million recorded for the expected cost of repairing defective subcomponents.

Services gross margin for 2006 was 59.1% compared to 67.5% for 2005. In 2005, our business grew more rapidly than our level of support personnel could support at the time. This resulted in relatively high margins with respect to services during 2005. In 2006, we made a planned increase to our services personnel headcount to support not only the increase in customer installed base in 2005, but also the anticipated increase in our installed base from our future business. This resulted in a relative decline in gross margins in 2006.

Research and Development. Research and development expense was \$37.2 million for 2006, or 21.1% of net revenues, compared to \$30.7 million in the comparable period of 2005, or 31.3% of net revenues. The \$6.5 million increase was primarily due to increased compensation costs of \$4.7 million attributable to an increase in employee headcount and \$1.4 million attributable to increased sub-contractor expenses. Research and development expense included stock-based compensation expense of \$1.0 million and \$0.5 million during 2006 and 2005, respectively.

Sales and Marketing. Sales and marketing expense was \$29.5 million, or 16.7% of net revenues, for 2006 compared to \$22.7 million, or 23.2% of net revenues, during 2005. The \$6.8 million increase was primarily due to increased compensation costs of \$4.6 million resulting from increased commissions and salaries, as well as increased headcount in support of our overall growth. In addition, travel and entertainment cost increased by \$0.9 million. Sales and marketing expense included stock-based compensation expense of \$0.6 million and \$0.3 million during 2006 and 2005, respectively.

General and Administrative. General and administrative expense was \$13.2 million, or 7.5% of net revenues, for 2006 compared to \$7.0 million, or 7.1% of net revenues, during 2005. The \$6.2 million increase was primarily due to increased compensation costs of \$2.5 million attributable to an increase in employee headcount, including additional accounting and finance personnel, an increase of \$2.6 million in spending related to our preparation for becoming a public company, including consulting costs associated with Sarbanes-Oxley compliance and improvement to our ERP systems, and \$0.8 million in costs associated with our audit committee's independent investigation of the accounting for revenue in our China operations. General and administrative expense included stock-based compensation expense of \$0.5 million and \$0.2 million during 2006 and 2005, respectively.

Other Expense, Net. Other expense, net includes interest income, interest expense and other expense, net and was \$1.4 million in 2006, compared to \$1.7 million in 2005. Other expense, net consisted primarily of expenses associated with changes in the fair value of our outstanding preferred stock warrants, interest expense and interest income. The change in other expense, net was primarily due to the adoption of FSP 150-5 on July 1, 2005, which resulted in a \$1.5 million expense arising from the increase in value of preferred stock warrants during the 2006 period. This compares to a \$0.1 million expense from the increase in value of preferred stock warrants during 2005. These increases were partially offset by \$0.6 million of remaining proceeds received upon satisfaction of an escrow condition on the sale of an investment obtained in conjunction with our BAS acquisition.

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Provision for Income Taxes. We incurred U.S. operating losses in all years from inception through 2005. Because of net operating loss carryforwards in the United States, the provision for income taxes of \$2.5 million and \$0.3 million for 2006 and 2005, respectively, were primarily related to provisions for foreign income taxes. For the year ended December 31, 2006, \$1.3 million of the provision for income taxes was related to the conclusion of a tax audit in Israel. The resolution of the audit resulted in amounts being due which were in excess of the amounts estimated and in excess of amounts previously recorded. The \$1.3 million includes the effects for the years ended December 31, 1999 through 2003 that were covered by the tax audit and the expected effect for the years ended December 31, 2004 through 2006 based on the outcome of the tax audit. As of December 31, 2006, we had net operating loss carryforwards for federal and state income tax purposes of \$93.8 million and \$46.0 million, respectively. We also had federal research and development tax credit carryforwards of approximately \$2.4 million and state research and development tax credit carryforwards of approximately \$2.3 million. Realization of deferred tax assets is dependent upon future earnings, if any, the timing and amount of which is uncertain. Accordingly, the net deferred tax assets arising from U.S. operations have been fully offset by a valuation allowance. If not utilized, the federal net operating loss and tax credit carryforwards will expire between 2019 and 2026, and the state net operating loss and tax credit carryforward will expire between 2008 and 2026. Utilization of these net operating losses and credit carryforwards will likely be subject to an annual limitation due to the provisions of Section 382 of the Internal Revenue Code.

Years Ended December 31, 2005 and 2004

Net Revenues. Net revenues for 2005 were \$98.0 million compared to \$35.5 million for 2004, an increase of \$62.5 million, or 176.1%. During 2005, revenues from our top five customers comprised 69% of net revenues, compared with 61% of net revenues during 2004. During 2005, revenues from customers in the United States comprised 83% of net revenues, and revenues from customers outside the United States comprised 17% of net revenues, compared to 2004 in which customers in the United States comprised 80% of net revenues, and revenues from customers outside the United States comprised 20% of net revenues.

Products revenues for 2005 were \$86.0 million compared to \$31.5 million for 2004, an increase of \$54.5 million, or 173.0%. The increase was primarily due to a \$44.7 million increase in revenue from our data products based on the inclusion of a full year of results from data products that we acquired in the BAS acquisition in June 2004. This \$44.7 million increase also includes revenues of \$18.8 million resulting from the timing of revenue recognition in 2005 associated with product previously shipped to a single customer in 2004 that was pending customer acceptance criteria. The increase in products revenues was also due to a \$9.7 million increase in revenues of our video products, primarily due to the broader adoption of our Digital Simulcast product and the initial deployment of our Switched Broadcast product application.

Services revenues for 2005 were \$12.0 million compared to \$3.9 million in 2004, an increase of \$8.1 million, or 207.7%. This \$8.1 million increase was primarily due to a larger installed base of products, including the installed base of products acquired in the BAS transaction.

Gross Profit/Gross Margin. Gross profit for 2005 was \$38.1 million compared to \$12.0 million for 2004, an increase of \$26.1 million, or 217.5%. Gross margin increased to 38.9% in 2005 compared to 33.7% in 2004.

Products gross margin for 2005 was 34.9% compared to 32.5% for 2004. Products gross margin in 2005 and 2004 were adversely impacted by the sale of inventory acquired in the BAS transaction. Under purchase accounting, the carrying value of this inventory was increased by \$4.7 million in June 2004, the date of acquisition, to the then fair market value. This inventory was sold in 2005 and 2004 reducing gross profit in those periods by \$3.5 million and \$1.2 million, respectively. This reduced product gross margin by 4.1% in 2005 and 3.8% in 2004. In addition, gross margin in 2005 decreased as a result of a physical inventory write-down of \$1.8 million and specific warranty provisions of \$1.5 million recorded for the expected cost of repairing defective subcomponents.

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Services gross margin for 2005 was 67.5% compared to 43.6% for 2004. Services gross margin was adversely impacted in 2004 by a \$0.7 million reduction to deferred services revenues arising from the application of purchase accounting for services contracts acquired in the BAS acquisition. The remainder of the increase in services gross margin in 2005 was primarily due to economies of scale arising from a larger installed base of video products and data products, due in part to the installed base of products acquired in connection with the BAS acquisition.

Research and Development. Research and development expense was \$30.7 million in 2005, or 31.3% of net revenues, compared to \$21.6 million in 2004, or 60.8% of net revenues. The \$9.1 million increase was primarily due to increased compensation costs of \$6.6 million attributable to an increase in headcount, \$1.8 million in increased depreciation of computer and lab equipment, a portion of which was acquired in the BAS acquisition, and \$0.5 million attributable to increased contractor expenses. During 2005, we received \$0.4 million in payments for non-recurring engineering that offset research and development expenses, compared to zero in 2004. Research and development expense included stock-based compensation expense of \$0.5 million and \$0.3 million during 2005 and 2004, respectively.

Sales and Marketing. Sales and marketing expense was \$22.7 million, or 23.2% of net revenues, in 2005 compared to \$15.9 million, or 44.8% of net revenues, in 2004. The \$6.8 million increase was primarily due to an increase of \$3.8 million in compensation costs arising from increased salaries and commissions, and an increase of \$0.9 million in travel expenses. Sales and marketing expense included stock-based compensation expense of \$0.3 million and \$0.1 million during 2005 and 2004, respectively.

General and Administrative. General and administrative expense increased to \$7.0 million, or 7.1% of net revenues, in 2005, from \$5.8 million, or 16.4% of net revenues, in 2004. This \$1.2 million increase was primarily due to an increase of \$1.7 million in compensation costs related to an increase in headcount, partially offset by a \$0.3 million decrease in consulting fees. General and administrative expense included stock-based compensation expense of \$0.2 million in each of 2005 and 2004, respectively.

In-Process Research and Development. We allocated a portion of the purchase price for the BAS acquisition to in-process research and development, which allocation is determined through established valuation techniques. In-process research and development represents an expense recorded for the portion of the purchase price of an acquisition allocated to research and development when technological feasibility of a research program has not been established and no future alternative uses exist at the time of acquisition. Total in-process research and development expense was \$1.0 million for the year ended December 31, 2004, which related primarily to ongoing software development efforts for the data products we acquired in connection with the BAS transaction.

Other Expense, Net. Other expense, net was \$1.7 million in 2005 compared to \$1.0 million in 2004. The increase was primarily due to an increase of \$0.7 million in interest expenses incurred on higher debt balances carried in 2005 compared to 2004, and \$0.5 million related primarily to foreign exchange losses. This increase in other expense, net was partially offset by an increase in interest income of \$0.5 million earned due to interest earned on relatively higher interest rates and relatively higher invested balances during 2005 compared to 2004.

Provision for Income Taxes. We incurred U.S. operating losses in 2005 and 2004. Because of the net operating loss carryforward in the United States, the provision for income tax for 2005 and 2004 was \$0.3 million in both periods reflecting provisions for foreign income taxes.

Cumulative Effect of Change in Accounting Principle. Upon adoption of FSP 150-5 on July 1, 2005, we reclassified the fair value of warrants from equity to a liability and recorded a cumulative effect of a change in accounting principle of \$0.6 million for 2005.

Table of Contents**Quarterly Results of Operations**

The following tables set forth selected unaudited quarterly consolidated statements of operations data for the last eight fiscal quarters, as well as the percentage that each line item represents of total net revenues. The information for each of these quarters has been prepared on the same basis as the audited consolidated financial statements included elsewhere in this prospectus and, in the opinion of management, includes all adjustments, consisting solely of normal recurring adjustments, necessary for the fair presentation of the results of operations for these periods. This data should be read in conjunction with the audited consolidated financial statements and related notes included elsewhere in this prospectus. These quarterly operating results are not necessarily indicative of our operating results for any future period.

	Quarters Ended							
	Mar 31, 2005	Jun 30, 2005	Sep 30, 2005	Dec 31, 2005	Mar 31, 2006	Jun 30, 2006	Sep 30, 2006	Dec 31, 2006
	(in thousands, except per share data)							
Consolidated Statements of Operations Data:								
Net revenues								
Products	\$16,619	\$25,944	\$20,210	\$23,193	\$27,974	\$32,245	\$37,094	\$56,700
Services	<u>2,788</u>	<u>3,035</u>	<u>2,652</u>	<u>3,538</u>	<u>4,576</u>	<u>5,763</u>	<u>5,970</u>	<u>6,302</u>
Total net revenues	<u>19,407</u>	<u>28,979</u>	<u>22,862</u>	<u>26,731</u>	<u>32,550</u>	<u>38,008</u>	<u>43,064</u>	<u>63,002</u>
Cost of net revenues								
Products	9,054	20,287	12,475	14,117	13,884	17,220	18,382	24,666
Services	<u>774</u>	<u>922</u>	<u>893</u>	<u>1,311</u>	<u>2,016</u>	<u>2,280</u>	<u>2,393</u>	<u>2,556</u>
Total cost of net revenues	<u>9,828</u>	<u>21,209</u>	<u>13,368</u>	<u>15,428</u>	<u>15,900</u>	<u>19,500</u>	<u>20,775</u>	<u>27,222</u>
Gross profit								
Products	7,565	5,657	7,735	9,076	14,090	15,025	18,712	32,034
Services	<u>2,014</u>	<u>2,113</u>	<u>1,759</u>	<u>2,227</u>	<u>2,560</u>	<u>3,483</u>	<u>3,577</u>	<u>3,746</u>
Total gross profit	<u>9,579</u>	<u>7,770</u>	<u>9,494</u>	<u>11,303</u>	<u>16,650</u>	<u>18,508</u>	<u>22,289</u>	<u>35,780</u>
Operating expense								
Research and development	7,879	7,274	7,652	7,896	8,320	8,964	9,316	10,594
Sales and marketing	5,212	5,402	5,574	6,541	6,757	7,163	7,045	8,558
General and administrative	1,497	1,744	1,897	1,846	2,527	2,599	2,922	5,128
Amortization of intangible assets	<u>143</u>	<u>143</u>	<u>143</u>	<u>144</u>	<u>143</u>	<u>143</u>	<u>143</u>	<u>143</u>
Total operating expense	<u>14,731</u>	<u>14,563</u>	<u>15,266</u>	<u>16,427</u>	<u>17,747</u>	<u>18,869</u>	<u>19,426</u>	<u>24,423</u>
Operating income (loss)	<u>(5,152)</u>	<u>(6,793)</u>	<u>(5,772)</u>	<u>(5,124)</u>	<u>(1,097)</u>	<u>(361)</u>	<u>2,863</u>	<u>11,357</u>
Other income (expense), net	<u>(444)</u>	<u>(293)</u>	<u>(380)</u>	<u>(579)</u>	<u>(223)</u>	<u>(361)</u>	<u>(904)</u>	<u>128</u>
Net income (loss) before provision for income taxes and cumulative effect of change in accounting principle	<u>(5,596)</u>	<u>(7,086)</u>	<u>(6,152)</u>	<u>(5,703)</u>	<u>(1,320)</u>	<u>(722)</u>	<u>1,959</u>	<u>11,485</u>
Provision (benefit) for income taxes	<u>96</u>	<u>104</u>	<u>62</u>	<u>63</u>	<u>(257)</u>	<u>(141)</u>	<u>381</u>	<u>2,542</u>
Net income (loss) before cumulative effect of change in accounting principle	<u>(5,692)</u>	<u>(7,190)</u>	<u>(6,214)</u>	<u>(5,766)</u>	<u>(1,063)</u>	<u>(581)</u>	<u>1,578</u>	<u>8,943</u>
Cumulative effect of change in accounting principle	<u>—</u>	<u>—</u>	<u>633</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>
Net income (loss)	<u><u>\$ (5,692)</u></u>	<u><u>\$ (7,190)</u></u>	<u><u>\$ (6,847)</u></u>	<u><u>\$ (5,766)</u></u>	<u><u>\$ (1,063)</u></u>	<u><u>\$ (581)</u></u>	<u><u>\$ 1,578</u></u>	<u><u>\$ 8,943</u></u>
Net income (loss) per common share, basic	<u><u>\$ (0.54)</u></u>	<u><u>\$ (0.67)</u></u>	<u><u>\$ (0.63)</u></u>	<u><u>\$ (0.52)</u></u>	<u><u>\$ (0.09)</u></u>	<u><u>\$ (0.05)</u></u>	<u><u>\$ 0.14</u></u>	<u><u>\$ 0.76</u></u>
Net income (loss) per common share, diluted	<u><u>\$ (0.54)</u></u>	<u><u>\$ (0.67)</u></u>	<u><u>\$ (0.63)</u></u>	<u><u>\$ (0.52)</u></u>	<u><u>\$ (0.09)</u></u>	<u><u>\$ (0.05)</u></u>	<u><u>\$ 0.03</u></u>	<u><u>\$ 0.15</u></u>

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	Quarters Ended							
	Mar 31, 2005	Jun 30, 2005	Sep 30, 2005	Dec 31, 2005	Mar 31, 2006	Jun 30, 2006	Sep 30, 2006	Dec 31, 2006
	(in percent)							
Consolidated Statements of Operations Data:								
Net revenues								
Products	85.6%	89.5%	88.4%	86.8%	85.9%	84.8%	86.1%	90.0%
Services	<u>14.4</u>	<u>10.5</u>	<u>11.6</u>	<u>13.2</u>	<u>14.1</u>	<u>15.2</u>	<u>13.9</u>	<u>10.0</u>
Total net revenues	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>
Cost of net revenues								
Products	46.6	70.0	54.6	52.8	42.6	45.3	42.6	39.2
Services	<u>4.0</u>	<u>3.2</u>	<u>3.9</u>	<u>4.9</u>	<u>6.2</u>	<u>6.0</u>	<u>5.6</u>	<u>4.1</u>
Total cost of net revenues	50.6	73.2	58.5	57.7	48.8	51.3	48.2	43.3
Gross profit								
Products	39.0	19.5	33.8	34.0	43.3	39.5	43.5	50.9
Services	<u>10.4</u>	<u>7.3</u>	<u>7.7</u>	<u>8.3</u>	<u>7.9</u>	<u>9.2</u>	<u>8.3</u>	<u>5.9</u>
Total gross profit	<u>49.4</u>	<u>26.8</u>	<u>41.5</u>	<u>42.3</u>	<u>51.2</u>	<u>48.7</u>	<u>51.8</u>	<u>56.8</u>
Operating expense								
Research and development	40.6	25.1	33.5	29.5	25.6	23.6	21.6	16.8
Sales and marketing	26.9	18.6	24.4	24.5	20.8	18.8	16.4	13.6
General and administrative	7.7	6.1	8.3	7.0	7.7	6.8	6.8	8.2
Amortization of intangible assets	<u>0.7</u>	<u>0.5</u>	<u>0.6</u>	<u>0.5</u>	<u>0.4</u>	<u>0.4</u>	<u>0.3</u>	<u>0.2</u>
Total operating expense	<u>75.9</u>	<u>50.3</u>	<u>66.8</u>	<u>61.5</u>	<u>54.5</u>	<u>49.6</u>	<u>45.1</u>	<u>38.8</u>
Operating income (loss)	(26.5)	(23.5)	(25.3)	(19.2)	(3.3)	(0.9)	6.7	18.0
Other income (expense), net	<u>(2.3)</u>	<u>(0.9)</u>	<u>(1.5)</u>	<u>(2.2)</u>	<u>(0.8)</u>	<u>(1.0)</u>	<u>(2.1)</u>	<u>0.2</u>
Net income (loss) before provision for income taxes and cumulative effect of change in accounting principle	(28.8)	(24.4)	(26.8)	(21.4)	(4.1)	(1.9)	4.6	18.2
Provision (benefit) for income taxes	<u>0.5</u>	<u>0.4</u>	<u>0.3</u>	<u>0.2</u>	<u>(0.8)</u>	<u>(0.4)</u>	<u>0.9</u>	<u>4.0</u>
Net income (loss) before cumulative effect of change in accounting principle	(29.3)	(24.8)	(27.1)	(21.6)	(3.3)	(1.5)	3.7	14.2
Cumulative effect of change in accounting principle	<u>—</u>	<u>—</u>	<u>2.8</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>
Net income (loss)	<u>(29.3)%</u>	<u>(24.8)%</u>	<u>(29.9)%</u>	<u>(21.6)%</u>	<u>(3.3)%</u>	<u>(1.5)%</u>	<u>3.7%</u>	<u>14.2%</u>

Our net revenues and cost of net revenues have generally increased sequentially during the last eight quarters. However, during the second quarter of 2005, we experienced an unusual increase in product net revenues from data products primarily due to \$18.8 million of revenues recognized in 2005 following satisfaction of customer acceptance criteria for product shipped to a single customer in 2004. Our net revenues during the fourth quarter of 2006 increased significantly on a sequential basis primarily due to accelerated product purchases in the fourth quarter by certain of our major customers in anticipation of their planned service implementations expected to occur in 2007, as well as customer spending related to the end of annual budgetary cycles. While we expect first quarter 2007 net revenues to increase compared to the same period in 2006, we expect first quarter 2007 revenues to decrease sequentially compared to the fourth quarter of 2006.

Gross margins have fluctuated on a quarterly basis primarily due to mix shifts between video and data products and between the hardware and software content of our products. In addition, gross margins have been impacted by the timing of physical inventory write-downs, the timing of specific inventory and warranty provisions and the timing of sales and cost of sales associated with inventory acquired in connection with the BAS acquisition. For example, the first and second quarters of 2005 were impacted by the write-off of inventory resulting from book to physical adjustments of \$1.2 million and \$0.6 million, respectively. The third quarter of 2006 was negatively impacted by a provision of \$0.8 million for excess and obsolete inventory during that

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quarter. The third and fourth quarters of 2005 were impacted by specific warranty provisions recorded during those periods of \$0.8 million and \$0.7 million, respectively, for the estimated cost of repairing defective subcomponents. The cost of net revenues and gross margins during the second quarter of 2005 were negatively affected by \$3.5 million or 11.9%, respectively, related to the sale of inventory acquired in connection with our BAS acquisition. Gross margins in the fourth quarter of 2006 were positively impacted by the relatively large, incremental product purchases during the quarter described above, a large, one-time software purchase that occurred during the fourth quarter and improved manufacturing overhead utilization arising from the significant increase in revenues during the period. We expect first quarter 2007 gross margins to decrease sequentially compared to the fourth quarter of 2006.

Operating expense has generally increased sequentially due to the growth of our business. Our research and development expense in the first quarter of 2005 was impacted by increased costs associated with CableLabs certification efforts relating to our data products. Our sales and marketing expense in the fourth quarter of 2005 was impacted by increased sales headcount and higher overall commissions as a result of our growth. Our general and administrative expense in the first quarter of 2006 was impacted by consulting fees related to information systems and preparation for Sarbanes-Oxley compliance. Our general and administrative expense in the fourth quarter of 2006 was adversely impacted by the hiring of new employees, costs related to our audit committee's independent investigation and consulting costs relating to preparation for our year-end audit and efforts we made during the quarter to complete the remediation of material weaknesses related to our 2004 and 2005 financial statement audits.

In the third quarter of 2005, we adopted FSP 150-5, which requires us to classify the warrants on our preferred stock as liabilities and adjust our warrant instruments to fair value at each reporting period. We recorded a \$0.6 million cumulative effect charge for adoption as of July 1, 2005, reflecting the fair value of the warrants as of that date, and \$56,000, \$56,000, \$85,000, 36,000, \$1.3 million and \$112,000 of additional expense that was recorded in other expense, net in the quarters ended September 30, 2005, December 31, 2005, March 31, 2006, June 30, 2006, September 30, 2006 and December 31, 2006, respectively, to reflect the increase in fair value of the warrants.

In the fourth quarter of 2006, our provision for income taxes included \$1.3 million related to the resolution of a tax audit in Israel, which was different than our estimates and in excess of the amounts previously recorded. The \$1.3 million includes the effect for the years ended December 31, 1999 through 2003 that were covered by the tax audit and the expected effects for the years ended December 31, 2004 through 2006 based on the outcome of the tax audit.

Our quarterly results of operations have varied in the past and are likely to do so again in the future. As such, we believe that period-to-period comparisons of our operating results should not be relied upon as an indication of future performance. In future periods, the market price of our common stock could decline if our revenue and results of operations are below the expectations of analysts or investors.

Liquidity and Capital Resources

Since inception, we have financed our operations primarily through private sales of equity and from borrowings under credit facilities, and more recently from cash flow from operations. At December 31, 2006, our cash, cash equivalents and marketable securities totaled \$65.5 million.

Operating Activities

Our operating activities generated cash in the amount of \$48.8 million for the year ended December 31, 2006, primarily due to net income of \$8.9 million, a decrease in inventory of \$14.4 million and an increase in deferred revenues of \$21.8 million, an increase in accrued and other liabilities of \$7.3 million, and an increase in accounts payable of \$6.3 million. These changes resulted primarily from the significant growth in our business, the timing of shipments and payments to vendors, our efforts to manage and monitor inventory balances and the

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increase in deferred revenue due to the timing of revenue recognition under our revenue recognition policy. The 2006 decrease in inventory compared to 2005 resulted from a more significant emphasis on efficiently managing our inventory levels through working with our suppliers. These changes were partially offset by an increase in trade receivables of \$19.3 million due to the growth in our business. We also had non-cash charges of \$10.6 million, comprised primarily of \$6.1 million in depreciation on property and equipment, \$2.5 million in stock-based compensation expense and \$1.5 million related to the increase in fair value of preferred stock warrants during the period.

Our operating activities generated cash in the amount of \$1.4 million in the year ended December 31, 2005, primarily due to an increase in deferred revenues of \$18.7 million and an increase in other accrued liabilities of \$2.7 million. These changes resulted primarily from the growth in our business, the timing of shipments and the satisfaction of revenue recognition criteria under our revenue recognition policy. Operating cash flow was also favorably affected by a decrease in trade receivables of \$6.1 million due to the timing of collections. These changes were largely offset by a loss of \$25.5 million, an increase in inventory of \$7.7 million, an increase in prepaid and other assets of \$1.3 million and a decrease in accounts payable of \$1.5 million due to the timing of payments to vendors. We also had non-cash charges of \$9.0 million, comprised primarily of \$5.9 million in depreciation on property and equipment, \$1.1 million in stock-based compensation expense and \$0.7 million related to the increase in value of preferred stock warrants during the period.

Our operating activities used cash in the amount of \$21.5 million in the year ended December 31, 2004, primarily due to a net loss during the period of \$33.8 million and an increase in trade receivables of \$15.0 million. The increase in trade receivables was largely due to the timing of a large shipment of data products to a specific customer, which occurred late in 2004. These items were partially offset by a decrease in inventory of \$9.4 million due to the increase in shipments to customers late in the year and an increase in deferred revenues of \$7.5 million. We also had non-cash charges of \$5.4 million, comprised primarily of \$3.2 million in depreciation on property and equipment and \$1.0 million related to in-process research and development charges.

Investing Activities

Our investing activities used cash of \$30.2 million in the year ended December 31, 2006, primarily from net purchases of marketable securities of \$20.0 million and the purchase of property and equipment of \$10.9 million to support the growth in our business. These capital expenditures consisted primarily of computer and test equipment and software purchases.

Our investing activities used cash of \$7.7 million in the year ended December 31, 2005, primarily from net purchases of marketable securities of \$6.9 million and the purchase of property and equipment of \$6.0 million. These capital expenditures consisted primarily of computer and test equipment and software purchases. These uses of funds for investing activities were partially offset by \$5.3 million in proceeds from the sale of an investment acquired in connection with the BAS acquisition in 2004.

Our investing activities used cash of \$2.8 million in the year ended December 31, 2004 primarily due to the purchases of property, plant and equipment of \$1.4 million to support growth in our business and net payments of \$1.5 million for the BAS acquisition. The capital expenditures consisted primarily of computer and test equipment and software purchases.

Financing Activities

Our financing activities provided cash of \$2.7 million in the year ended December 31, 2006, primarily from a net increase in borrowings of \$2.8 million, and proceeds of \$0.8 million received from the exercise of options to purchase our common stock, offset by \$0.7 million of payment of costs to professional service providers associated with our preparation for our initial public offering.

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Our financing activities used cash of \$0.2 million in the year ended December 31, 2005, primarily from repayments of loans and payments against capital lease obligations of \$0.7 million, offset by proceeds of \$0.5 million received from the exercise of options to purchase our common stock.

Our financing activities provided cash of \$33.7 million in the year ended December 31, 2004, principally due to the sale of our preferred stock of \$25.1 million, the exercise of warrants to purchase our common stock of \$1.9 million and proceeds from net borrowings of \$7.4 million.

Our revolving credit facility with Silicon Valley Bank provides up to \$10.0 million in the form of a term loan and up to \$20.0 million for working capital requirements. As of December 31, 2006, \$10.0 million was outstanding under the term loan and \$4.0 million was outstanding under the revolving credit facility for working capital. The term loan bears interest at the Federal Reserve's prime rate plus 0.25%, and the revolving credit facility bears interest at the Federal Reserve's prime rate. The loan is collateralized by all of our tangible assets. The loan agreement contains financial and non-financial covenants including maintaining a "tangible net worth," as defined in the credit facility, of at least negative \$6.0 million. Through December 31, 2006, we were in compliance with all covenants. We expect to use approximately \$14.0 million of the net proceeds of this offering to repay outstanding debt under our term loan and the revolving credit facility.

We believe that our existing cash and cash equivalents and existing amounts available under our revolving credit facility, together with the net proceeds from this offering, will be sufficient to meet our anticipated cash needs for at least the next twelve months. Our future capital requirements will depend on many factors including our rate of revenue growth, the timing and extent of spending to support development efforts, the expansion of sales and marketing activities, the timing of introductions of new products and enhancements to existing products, the costs to ensure access of adequate manufacturing capacity and the continuing market acceptance of our products. In the event that additional financing is required from outside sources, we may not be able to raise it on terms acceptable to us or at all. If we are unable to raise additional capital when desired, our business, operating results and financial condition would be harmed.

Contractual Obligations and Commitments

The following summarizes our contractual obligations at December 31, 2006

	Payments Due by Period (in thousands)				
	Total	Less Than 1 Year	1 -3 Years	3 -5 Years	Thereafter
Operating lease obligations	\$ 9,705	\$ 2,574	\$ 5,085	\$ 2,046	\$ —
Capital lease obligations	63	27	36	—	—
Notes payable ⁽¹⁾	14,480	1,913	12,567	—	—
Interest payments ⁽²⁾	1,977	1,180	797	—	—
Total	<u>\$26,225</u>	<u>\$ 5,694</u>	<u>\$ 18,485</u>	<u>\$ 2,046</u>	<u>\$ —</u>

(1) The notes payable to Silicon Valley Bank were refinanced on August 18, 2006. We expect to repay these notes in their entirety with a portion of the net proceeds from this offering.

(2) Represents estimated interest payments on our debt using an interest rate of 8.41% at December 31, 2006.

Off-Balance Sheet Arrangements

As of December 31, 2006, we have no off-balance sheet arrangements as defined in Item 303(a)(4) of the Securities and Exchange Commission's Regulation S-K.

Effects of Inflation

Our monetary assets, consisting primarily of cash, marketable securities and receivables, are not affected by inflation because they are short-term and in the case of cash are immaterial. Our non-monetary assets, consisting

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primarily of inventory, intangible assets, goodwill and prepaid expenses and other assets, are not affected significantly by inflation. We believe that the impact of inflation on replacement costs of equipment, furniture and leasehold improvements will not materially affect our operations. However, the rate of inflation affects our cost of goods sold and expenses, such as those for employee compensation, which may not be readily recoverable in the price of products and services offered by us.

Recent Accounting Pronouncements

See Note 2 of the Notes to Consolidated Financial Statements included in this prospectus for recent accounting pronouncements that could have an effect on us.

Quantitative and Qualitative Disclosures about Market Risk***Interest Rate Sensitivity***

The primary objectives of our investment activity are to preserve principal, provide liquidity and maximize income without significantly increasing risk. Some of the securities we invest in are subject to market risk. This means that a change in prevailing interest rates may cause the principal amount of the investment to fluctuate. To minimize this risk, we maintain our portfolio of cash equivalents and short-term investments in a variety of securities, including commercial paper, money market funds, government and non-government debt securities and certificates of deposit. The risk associated with fluctuating interest rates is limited to our investment portfolio. A 10% decrease in interest rates in 2005 and 2006, would result in a decrease in our interest income of \$63,000 and \$153,000, respectively. As of December 31, 2006, our investments were in commercial paper, corporate notes and bonds, market auction preferred stock and U.S. government securities.

Our exposure to interest rates also relates to the increase or decrease in the amount of interest we must pay on our outstanding variable rate debt instruments, primarily certain borrowings under our revolving credit facility. Our revolving credit facility provides financing up to \$20.0 million for working capital requirements and \$10.0 million under the term facility. As of December 31, 2006, \$10.0 million was outstanding under the term loan facility and \$4.0 million was outstanding under the revolving credit facility. The loans bear interest at the Federal Reserve's prime rate for the revolving credit facility and at the Federal Reserve's prime rate plus 0.25% per annum under the term facility. A 10% increase in the prime rate would result in an increase in interest expense of \$0.1 million on an annual basis.

Foreign Currency Risk

Our sales contracts are primarily denominated in United States dollars and therefore the majority of our net revenues are not subject to foreign currency risk. Our operating expense and cash flows are subject to fluctuations due to changes in foreign currency exchange rates, particularly changes in the Euro. To date, we have not entered into any hedging contracts since exchange rate fluctuations have had little impact on our operating results and cash flows.